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COMPETITION BETWEEN SMALL BUSINESS AND PUBLIC UTILITIES

HEARING

BEFORE THE

SUBCOMMITTEE ON ANTITRUST AND RESTRAINT
OF TRADE ACTIVITIES AFFECTING
SMALL BUSINESS

OF THE

COMMITTEE ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES

NINETY-EIGHTH CONGRESS

SECOND SESSION

WASHINGTON, DC, MAY 22, 1984

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COMPETITION BETWEEN SMALL BUSINESS AND PUBLIC UTILITIES

TUESDAY, MAY 22, 1984

HOUSE OF REPRESENTATIVES, SUBCOMMITTEE ON ANTI-
TRUST AND RESTRAINT OF TRADE ACTIVITIES AFFECTING
SMALL BUSINESS, COMMITTEE ON SMALL BUSINESS,
Washington, DC.

The subcommittee met, pursuant to notice, at 1 p.m., in room 2359-A, Rayburn House Office Building, Hon. Thomas A. Luken (chairman of the subcommittee) presiding.

OPENING STATEMENT OF CHAIRMAN LUKEN

Mr. LUKEN. The subcommittee will come to order.

This hearing will examine regulated monopolies competition with small business.

The question of unfair competition between small business and public utilities apparently is a serious one. Small business witnesses will testify here, as they have on many occasions, that public utility companies in the United States are using their special status to compete with them installing and servicing heating and cooling systems, electrical, and gas appliances.

As a member of the House Energy and Commerce Committee, I am certainly familiar with the public utility industry and the challenges which it now confronts.

Today this subcommittee will study the impact on small businesses of the utilities' efforts to meet these challenges through diversification.

Since the oil shocks of the 1970's, consumers have become more conscious of conserving energy. Everyone wants to lower his or her gas and electric bills with energy-saving methods. Utilities have begun to meet this need by diversifying into many services which have been traditionally performed by small contractors.

Some of this diversification is a result of the Residential Conservation Service Program or RCS. We want to see what effect this diversification is having on the various small businesses involved.

There is a public policy question here before this committee, and that is whether competition is healthy for the marketplace or if there are, in fact, inherent advantages for utilities—the regulated monopoly—because of their monopoly status, that make it difficult for small business to compete.

We will be examining several issues today including whether State and Federal law is adequate to address these small business

concerns and also considering the impact of these activities on the utility ratepayer.

Our witnesses today will include representatives of small contractors, utilities, the Small Business Administration, and the FTC.

We will proceed in a moment, but first the gentleman from Texas, Mr. Gonzalez, do you have any statement?

Mr. GONZALEZ. I have no statement. Thank you, Mr. Chairman.

Mr. LUKEN. All right. The first witness is Frank Swain, chief counsel for advocacy of the Small Business Administration.

**TESTIMONY OF FRANK S. SWAIN, CHIEF COUNSEL FOR
ADVOCACY, SMALL BUSINESS ADMINISTRATION**

Mr. SWAIN. Good afternoon, Mr. Chairman.

Mr. LUKEN. Your statement has been submitted in writing.

Mr. SWAIN. Yes, sir.

Mr. LUKEN. And, without objection, it will be received into the records of the committee. You may proceed in any way that you think will be helpful to us this morning.

Mr. SWAIN. Thank you, Mr. Chairman.

I would like to, rather than read the statement verbatim, summarize what I think are our particular points and concerns.

I thank you, Mr. Chairman, and the subcommittee, for the opportunity to address this important issue of utility competition with small business. The Office of Advocacy at the Small Business Administration has been interested in this issue for some time.

In March, my office issued a report entitled "Utility Competition with Small Businesses," which provides advice and guidance to State energy officials and other officials and small businesses on this complex issue.

Utilities engaged in unregulated businesses enjoy unique advantages over competing unregulated private firms through their government-granted monopoly status.

It is generally recognized that participation in unregulated markets by regulated entities, such as utilities, raises competition concerns, particularly with respect to the problem of cross subsidies between the regulated and the unregulated parts of the business.

For instance, the recent divestiture of certain AT&T businesses was based, in large part, on the recognition that cross subsidies between the unregulated and the regulated businesses within AT&T could not be eliminated through regulatory oversight.

Likewise, the Department of Justice has been actively seeking a removal of the cross-subsidization by the U.S. Postal Service of its electronic mail service, and there is some extensive material regarding that case attached to our statement. We did that because we think that the utility supply and installation programs raise identical unfair competition issues.

I'd like to basically address two issues for you this afternoon, Mr. Chairman, and just outline them, because I'm sure that the small business witnesses to follow will be much more articulate in their testimony and their specific examples than I can be.

We would basically like to discuss both the supply and installation and financing programs and the Commercial and Apartment Conservation Service—the CACS—program.

Concerning utility supply and installation, these programs cannot really be effectively regulated to absolutely eliminate improper subsidies and other competition problems.

Such unregulated activity by the utilities does not provide significant public benefits which outweigh the hazard to competition, especially to smaller firms, and the cost of regulatory oversight. Therefore, our office is on record recommending that utilities not be permitted to engage in this activity at all.

The reason for this is very simple. If a utility which is grossing literally millions of dollars in their major line of business—which is selling energy, power, or gas, or whatever the case may be—decides to get into the unregulated business of utility of supply and installation, that unregulated revenue probably is going to be fairly minor compared to their general source of revenue, and it may not raise major problems within the management of the utility. It may not raise major problems within the context of the local regulators that are charged with overseeing the activities of that utility.

However, the supply and installation programs of the utilities could be, and often are, a very significant portion of the local market and could cause great concern to the local small businesses.

Thus, while the danger to small business competition can be considerable, the potential adverse impact on the ratepayers is most often too small to warrant significant scrutiny by the Public Utility Commission staff, whose primary, if not sole, authority is to protect the ratepayers, not the small business competition.

Small business concern about utility supply programs goes beyond improper subsidies. A utility supply and installation program could still disrupt competitive markets by selection of particular products, suppliers, or installers, by unfairly promoting its own fuel or by setting product or service prices.

Based on the observations that we have made and the visits that we have had from people involved in the small business community in the affected industries, we recommend in our report that such programs be flatly prohibited by the various States.

As an alternative, at a minimum, we recommended that each such program that is proposed by local utilities be reviewed at public hearings at the State level to assure full public input into the program formulation process and that competition concerns be addressed.

We outline those concerns, but basically we want to make sure that when a utility decides to get into an unregulated business, that somebody is taking a look to make sure that that decision by that utility does not adversely affect competition and that there are not alternatives to that utility decision that may be less onerous on the local small business community.

We have several examples of cross subsidies in our statement and attachments. We do think it is a continuing and increasingly significant problem, and we think it is obviously something that the State regulators in particular have to take a look at.

We are not only talking about the subsidies—the financial subsidies—but also several of the proposals of the utilities to actually involve themselves in either doing the work themselves or in contractor selection.

We believe that if a utility would act as a referral service for private firms to supply and install the products, the financial drain on the utility as well as competition questions would be eliminated.

For example, we have been following a case in New Jersey in which New Jersey rejected a CACS utility supply and installation program in favor of a financing program offering loans at below market rates. I have little doubt that such a program would yield more requests for audits, more business for conservation suppliers and installers, and better attainment of energy goals at less cost to utilities.

The problems in the residential area, Mr. Chairman, are largely the same in the commercial area, which is, as you know, regulated under a different law, the Commercial and Apartment Conservation Service Program, enacted in 1980, I believe.

We point out in our report that the audit program called for under the CACS program threatens competition in several different markets.

I want to stress, as you did in your opening statement, that I think it is very good that the American public is becoming increasingly oriented toward energy conservation, but I don't think that there is anything in any of the laws that have been passed by the Congress over these last several years, including the Residential Conservation Service Program and the CACS program, which requires utilities themselves to get involved in the energy conservation business.

While it is true that utilities are required to offer energy audits under the CACS program, no Federal mandate exists to supply and install conservation products. So I don't think that any of the laws that have been passed are any excuse for the competition problems that we are seeing now between the large utilities and the smaller firms.

I think that utilities have an obligation, obviously, to work with the RCS and the CACS, but neither of those laws requires them to get into the supply and installation business. Neither of those Federal statutes ties up the utilities so tightly that they have to do everything themselves, as opposed to contracting out to smaller firms or act basically as a referral service.

I think ultimately the fact that U.S. consumers are more energy conscious should redound to the benefit not only of our national energy policy but of the firms, large and small, that are involved in the energy business.

What we are basically asking for is that the rules involving that energy business be absolutely clear and the same for all parties. The fact that utilities can come in with an inherent advantage and a protected rate base gives them, in many cases, a leg up. We think that, in particular, the local utility regulators have to bear that in mind.

I should add that we are aware that the House Energy and Commerce Committee is now considering a bill which corrects the oversight in the National Energy Conservation Policy Act, which omitted the prohibitions for supply and installation in the commercial market in the CACS program, as is already in the law in the RCS program.

So obviously that, from what we understand, it was primarily an oversight. But, by and large, it's an issue that we think the State regulators have to be particularly concerned with, and the small business community, if they make their voice known, and if they are able to document their case, ought to be able to get responsive action from the State regulatory offices.

I would like to mention that our report, which was sent to the various States, has been very well received, by and large. About half of the responses we have gotten have been favorable and sometimes asking us for follow-up information. Several other States indicated that they do not yet feel that this particular issue is a problem in their States.

I'm not sure that that's the case so much as the fact that local small businesses probably haven't gotten together with the State people to let them know their local concerns.

At any rate, we congratulate the committee for their continuing interest in this.

We do, in our testimony, outline a couple of approaches which we think are particularly good that various States have taken, and we look forward to continue the work with you, Mr. Chairman, and other members of the committee, interested officials, utilities, and small businesses, in considering how to solve this important issue.

We anticipate being part of an increasingly fruitful dialog to work together to address these energy goals and our small business concerns.

Thank you, Mr. Chairman.

[Mr. Swain's prepared statement with attachments follows:]

PREPARED STATEMENT OF FRANK S. SWAIN, CHIEF COUNSEL FOR ADVOCACY, SMALL BUSINESS ADMINISTRATION

Mr. Chairman, I thank you for the opportunity to address the important issue of utility competition with small business before the subcommittee. In March, I issued a report entitled "Utility Competition With Small Businesses" which provides guidance to state energy officials, utilities and small businesses on this complex issue.

BACKGROUND

Utilities engaged in unregulated businesses enjoy unique advantages over competing unregulated private firms through their government-granted monopoly status. It is generally recognized that participation in unregulated markets by regulated entities, such as utilities, raise competition concerns, particularly with respect to the problem of cross-subsidies between regulated and unregulated ventures. The recent divestiture of certain AT&T businesses was based, in large part, on the recognition that cross-subsidies between these regulated and unregulated businesses could not be eliminated through Federal regulatory oversight. The Department of Justice has been actively seeking a removal of the cross-subsidization by the Postal Service of its electronic mail service. In that case, the Department took the position that, "as a matter of public policy, E-COM [electronic mail] service should not be offered by the Postal Service because it inherently creates a substantial risk of impairing the competitive development of the electronic mail services industry as a result of cross-subsidization from the Postal Service's monopoly over First-Class Mail delivery."¹ Utility "supply and installation" programs² raise identical unfair competition issues.

¹ I have included as an appendix, two excerpts from the December 23, 1983 Department of Justice post-hearing brief in Postal Rate Commission Docket No. R83-1, explaining the impact of cross-subsidization by a regulated monopolist on unregulated markets.

² By "supply and installation" programs, I mean where the utility itself either supplies or installs the energy-related products, and not where the utility simply refers customers to a broad list of contractors and suppliers who deal directly with the consumer.

Our report generally addresses two areas: utility energy-related programs (supply and installation and financing programs) and the Commercial and Apartment Conservation Service (CACS) programs, the Federally-mandated energy audit program. I will briefly discuss the most significant recommendation in each area.

UTILITY SUPPLY AND INSTALLATION

Utility supply and installation programs cannot be effectively regulated to eliminate improper subsidies and other competition problems. Such unregulated activity by the utility does not provide significant public benefits which outweigh the hazard to competition and the cost of regulatory oversight. Therefore, the March report recommended that utilities not be permitted to engage in this activity.

Let me illustrate the difficulty of guarding against cross-subsidization of such programs with ratepayer funds. Typically, the revenue to a utility from the supply and installation programs is less than half of 1 percent of total utility revenues. Let me use the example of one Northeastern utility with roughly \$300 million in revenue, which receives about \$1 million from its appliance and energy conservation sales division. The public utility commission had not been reviewing whether the \$1 million sales operation was being subsidized, presumably because it did not have the interest or resources to review such a relatively small operation. In contrast, however, \$1 million of sales in the unregulated supply and installation business could be, and often is, a very significant portion of that business, and could cause great havoc in that market. Thus, while the danger to small business competition can be considerable, the potential adverse impact on the ratepayer is most often too small to warrant significant scrutiny by public utility commission staff (whose primary, if not sole, authority is to protect ratepayers, not small business competition).

Small business concern about supply and installation programs goes beyond improper subsidies. A utility supply and installation program could still disrupt competitive markets by its selection of particular products, suppliers or installers, by unfairly promoting its own fuel, or by setting product or service prices.

For the above reasons, we concluded that supply and installation programs pose significant competition problems. Further, we have not observed any significant benefits from such programs that cannot be provided by unregulated private firms. Indeed, we assert that properly structured utility financing programs, using some form of financial incentives, like those used by Tennessee Valley Authority, Pacific Power and Light and Southern California Gas, using the private firms are markedly better. Based on these observations and the impracticability of regulatory oversight, we recommended in our report that such programs be flatly prohibited by the states.

At a minimum, we recommended that each such program be reviewed at a public hearing at the state level to assure full public input into the program formulation process and that competition concerns be addressed. Such a public forum will benefit all such utility programs by assuring that: (1) the program most effectively addresses its energy goals; (2) the program does not adversely affect competition; and (3) alternative programs can be considered.

It has been suggested that there is no competition problem with existing utility supply and installation programs and that public hearings are not necessary. There are many examples of such problems, and where public hearings did or could have improved the utility program. I have attached brief descriptions of these examples to my testimony.

These examples are only a cross-section of the complaints received. I believe it is well demonstrated that all utility programs, particularly supply and installation programs should, at a minimum, be subject to some scrutiny at the local level. Furthermore, the evidence is considerable that utility supply and installation programs, unless severely limited in scope and time, and very well monitored, simply are not warranted by the meager public benefits provided by such program. As our report indicates, our first preference is to ban such programs, and our second preference is to monitor them through the local public hearing process.

Lastly, and most significantly from the utility perspective, we believe that our advice to shun supply and installation programs in favor of financing programs is more cost-effective for the ratepayer and the utility.³ It is not uncommon for supply and installation programs to lose money. If a utility would act as a referral service for private firms to supply and install the products, the financial drain on the utility would be eliminated and conservation goals would be achieved. For example, in

³ As the report discusses (pp. 3-6), financing programs, while preferred over supply and installation programs, also raise competitive concerns which require attention.

drafting its CACS program, New Jersey rejected a CACS utility supply and installation program in favor of a financing program offering loans 6 percent below market rates. I have little doubt that such a program would yield more requests for audits, more business or conservation suppliers and installers, and better attainment of energy goals at less cost to the utilities.

COMMERCIAL AND APARTMENT CONSERVATION SERVICE PROGRAM (CACS)

The other major significant set of recommendations made in the SBA report concern the Commercial and Apartment Conservation Service (CACS) Program being implemented by the states under regulations issued by the Department of Energy. We pointed out in our report that this audit program threatens competition in three different markets: (1) energy auditing; (2) supply and installation; and (3) other utilities and alternative fuel suppliers. The report recommends methods for structuring the program to avoid these competition problems.

Some argue that small businesses should not object to utility involvement in supply and installation of energy conservation products and in energy auditing (e.g., CACS). Specifically, it is contended that: (1) CACS should benefit small businesses because it will generate business for small business suppliers and installers; (2) Congress required utilities to get involved in the energy business; and (3) Congress intended that subsidized CACS audits be provided to further energy conservation goals.

First, we agree that small business suppliers and installers could benefit from CACS. Indeed, our comments at DOE on the Residential Conservation Service (RCS)⁴ and CACS programs over the last few years were directed at increasing small business participation by maximizing competition in these markets. Our report simply indicates that certain precautionary measures should be taken to assure that the benefits of CACS are not overwhelmed by its negative aspects.

Second, it is commonly asserted by utilities that Federal law requires them to get involved in the energy conservation business. While it is true that utilities are required to offer energy audits, no Federal mandate exists to supply and install conservation products. In fact, there is a general prohibition of supply and installation activities in the residential market subject to several narrow exemptions. The House Energy and Commerce Committee is now considering a bill, H.R. 4674, which corrects the oversight in the National Energy Conservation and Policy Act which omitted the analogous prohibitions in the commercial market. Thus, the general message of the Federal legislation is for utilities to stay out of supply and installation. Further, the Federal requirement to perform energy audits does not extend to the utility using the Federal program as a marketing opportunity for its own fuel and favored products.

Third, it has been argued that Congress intended that subsidized CACS audits be provided to promote conservation. As the SBA report indicates, the provision of the subsidy does unfairly disadvantage small business competitors who do not receive such a subsidy. Those who assert the subsidy is necessary do so on the basis that it is required to increase CACS audit requests by building owners and increase CACS program effectiveness. However, one can increase CACS audit effectiveness equally well, if not better, by providing financial incentives (e.g., rebates, low interest loans) to building owners with the audit. Additionally, to the extent a subsidy is deemed necessary, serious consideration should be given to contract out this activity to private unregulated firms (see report, p. 10). In sum, my office and the report do not oppose such a subsidy where necessary, and the report suggests alternatives which are less damaging to competition and may not require a subsidy.

The most important CACS audit program recommendation, is the general admonition to contract out the energy audit function, where practicable, to an independent entity. This recommendation is based on the conflict of interest between the utility as a provider of fuel or supplier and installer, and competing fuel suppliers and other suppliers and installers. For example, in the area of so-called "fuel switching", a gas utility has more than an academic interest in users of fuel oil switching to gas.

This problem recently surfaced in the Northeastern electric utility. It was fined \$600,000 by the state utility commission for failing to properly implement the state mandated energy audit program (analogous to RCS). This utility used ratepayer funds to subsidize the sale of electric heat pumps despite the fact that the installations were not deemed cost effective under the state program. Another gas utility in

⁴ The Residential Conservation Service (RCS) program is the federally-required utility residential energy audit program.

the same state has apparently been misusing the state audit program. Since 1977, this utility has provided the financing for only 4 oil furnace upgrades, while financing oil to gas conversions for over 2,300 homes, and gas furnace upgrades for over 1,100 homes. The homes audited were divided approximately equally between oil and gas heat. These examples illustrate the potential for audit programs to unfairly promote the use of the utility's fuel and related appliance over the competition. Thus, the utility competition problem is not restricted to utilities that have supply and installation programs, but potentially extends to all utilities that have audit programs (RCS or any other type).

The New York State Energy Office explicitly adopted this recommendation in the formulation of its CACS program and in draft legislation affecting all utility energy audit programs. The Governor of New York submitted legislation to establish a Statewide Energy Audit and Loan Program (SEAL) to replace the existing state audit program, presently run by the nine private utilities. A letter dated April 12, 1984 from the New York State Energy Commissioner, William D. Cotter, describing the legislation explains, "[b]y eliminating utility sponsorship of auditors, auditing services will be provided by entities without vested interests in promoting specific fuel types or specific equipment. We believe that this approach will be useful in reaching those most in need of energy conservation assistance with reliable unbiased information." New York will be required independent auditors also for the CACS program. Incidentally, New York has opted to increase CACS participation through the provision of attractive financing to apartment and building owners to upgrade their buildings.

RESPONSE OF THE STATES TO THE UTILITY REPORT

The utility report was sent in March to all the state CACS energy offices and state public utility commissions. We have received comments on the report from about a dozen states. Responses appear to be split in two ways. One half of the states indicate that they will seriously consider our recommendations. At this early date, a number of states have been adopting portions of our CACS recommendations. For example, the District of Columbia explicitly requested public comments on our CACS recommendations in the development of its plan.

The remaining states indicated that no competition problems have been observed in their state. We believe this response is explained by the lack of a significant problem in some states and/or by the widespread lack of small business interaction with state policymakers on this issue.

We are aware of two states with legislation pending that could serve as a model for other states. The Governor of New York proposed legislation on requiring the use of independent third parties for the energy audit function, as mentioned above. California is presently considering legislation (S.B. 1016) that will flatly bar utilities from performing contracting work on nonutility properties except in the performance of its utility function of generation, transmission or distribution of electricity, gas, water or steam. California adopted a law last year (Chapter 984 of Statutes of 1983) declaring the intent of the legislature that public utility regulation be based on the principle that the energy conservation industry should be allowed to develop in a competitive manner that is free from potential dominance by public utilities. Each of the above state approaches warrant serious consideration by other state officials interested in a small business-sensitive energy policy.

We look forward to working with interested officials, utilities and small business in considering our recommendations in the report. We anticipate being part of an increasingly fruitful dialogue for methods of working together to address these important energy goals and small business problems.

APPENDIX A

EXCERPTS FROM DOJ BRIEF

Before the
POSTAL RATE COMMISSION
Washington, D.C. 20268

E-COM Rate and Classification)
Changes, 1983)

Docket No. R83-1

INITIAL POST-HEARING BRIEF
OF THE UNITED STATES DEPARTMENT OF JUSTICE

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Antitrust Division

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December 23, 1983

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this proceeding under Section 3622(b)(9) of the Act. That section authorizes the Commission to consider "such other factors as [it] deems appropriate." 66/ The clear policy of Sections 3622(b)(4) and (b)(5) is that the Commission should specifically consider the effect of postal rates on private sector competition with the Postal Service. This policy can and should be applied here pursuant to Section 3622(b)(9).

2. Cross-Subsidization By A Regulated Monopolist Creates A Substantial Risk Of Impairing Competition And Of Monopolization Of Competitive Markets

Although prices can sometimes deviate from long-run incremental cost, in competitive markets such conduct simply cannot be sustained for more than a transitory period. Tr. 16/5333; Tr. 17/5424 (Owen). Pricing any product below its marginal cost requires a source of funds to make up the difference between cost and price. Sustained pricing below long-run incremental cost as a result of cross-subsidization is thus possible only by a firm that is, to some extent, protected from competition 67/ -- in other words, a firm that has the power to hold price above cost on one product and thus provide

66/ 39 U.S.C. § 3622(b)(9).

67/ Although in a competitive market a firm may successfully raise price somewhat above marginal cost, the market mechanism permits such a result only for a transitory period. Tr. 16/5166 (Owen). The effect of competition is that prices are driven down to cost. Id. at 5614.

a vehicle for cross-subsidization of a second, competitive product. 68/

The Private Express Statutes grant the Postal Service a congressionally sanctioned monopoly over regular First-Class Mail. 69/ The existence of this monopoly creates a significant threat of below-cost pricing in competitive markets like the E-COM market. Expansion by regulated monopolists into competitive markets has received a great deal of attention from economists. 70/ Unlike a traditional private firm, which may have the incentive to engage in short-run "predatory" below cost pricing as a means of driving rivals from the market, 71/ a statutory regulated monopolist, by virtue of its monopoly, has access to a permanent source of funds to finance below-cost sales in competitive markets. Indeed, the "celebrated" 72/ Averch-Johnson article made this distinction quite clearly.

The regulated firm can "afford" to take (long-run) losses in these second markets while competing firms cannot. . . . It may succeed.

68/ Sustained cross-subsidization is also possible by a firm, like the Postal Service, that can receive direct operating subsidies to cover total cost. Tr. 16/5233 (Owen).

69/ See 18 U.S.C. §§ 1693-99, 1724 (criminal); 39 U.S.C. §§ 601-06 (civil).

70/ These effects are detailed in Dr. Owen's direct testimony, Tr. 16/5164-76; see also Tr. 16/5207, and are confirmed by Dr. Willig in his rebuttal testimony, USPS-RT-5 at 12, 13-14.

71/ USPS-RT-5 at 13 (Willig).

72/ This is Dr. Willig's term. USPS-RT-5 at 14.

therefore, in either driving lower-cost firms out of these markets or of discouraging their entry into them. This is unlike the textbook case of "predatory price-cutting" where the regulated monopolist may temporarily cut prices in outside competitive markets to drive out rivals and subsequently raise prices to monopoly levels. The monopolist would ordinarily engage in such a practice only if he had the expectation that in the long run he would make a positive profit in these additional markets; but here even in the case of a long-run loss a regulated firm may find operations in such markets to be advantageous as long as the firm is permitted to include its capital input in these markets in its rate base. 73/

In short, the distinguishing feature of these situations is that where there is a regulated monopoly service or an external continuing source of subsidy, the below-cost pricing may be permanent, not temporary, so that the often doubtful issue as to whether prices can later be increased never arises. "[I]n some situations, a regulated enterprise may permanently set its prices below costs and keep them there." 74/

The ability of such firms to finance expansion into competitive markets with revenues and costs properly attributable to the monopoly services poses a distinct threat of harm to competition in the competitive markets and the clear likelihood of burdening monopoly ratepayers with the cost of

73/ Averch & Johnson, "Behavior Of The Firm Under Regulatory Constraint," 52 American Econ. Rev. 1052, 1058 (1962).

74/ USPS-RT-5 at 13-14 (Willig).

that expansion. Tr. 16/5168 (Owen). As Dr. Owen demonstrated in his direct testimony:

The USPS has the ability and may have the incentive to cross-subsidize its E-COM service at the expense of its monopoly services. The result will be an E-COM service priced below cost, creating an unjustifiable risk of injury to competitive services and to competition. New firms may be deterred from entering this market and the resulting distortion in resource allocation as prices depart from costs will reduce consumer welfare. . . . Ultimately, the new service [E-COM] may itself be monopolized.

Tr. 16/5168-69.

The fact that the Postal Service is not subject to a traditional rate-of-return constraint does not substantially alter this analysis. First, like a firm regulated through an allowed rate-of-return, absent regulatory intervention the Postal Service can misallocate costs to its monopoly services. ^{75/} Second, the fact that the Postal Service is not a traditional profit-maximizing firm increases the likelihood that Postal Service management may make marketing decisions on the basis of managerial objectives besides profits, such as the size and stature of the organization itself or the glamour of

^{75/} The Postal Service's break-even constraint is, in effect, a rate-of-return constraint with the allowed rate-of-return set equal to the cost of capital. Tr. 16/4964 (Owen). Notwithstanding witness Driscoll's argument that the cost of capital to the Postal Service is zero, see USPS-RT-4 at 16, it is clear that the Postal Service has considerable outstanding debt obligations that are included in its revenue requirement. See p. 56 infra.

participating in "high-tech" ventures. Tr. 16/5174-75 (Owen). In a competitive market, such behavior would lower profits, providing managers with strong economic incentives to avoid it. Id. at 5175. Furthermore, the inclusion of profitability as one among a number of managerial objectives in the usual regulated utility case limits the extent to which other, "subjective" objectives can be pursued. Id. As a result, the presumed absence of a profit-maximization motive on the part of USPS management in fact eliminates a check on discretionary managerial objectives that might otherwise exist, and provides an independent incentive for expansion into competitive, traditionally private sector activities. 76/

The effects of cross-subsidization of competitive services by a regulated monopolist are well-documented in the record. 77/ These effects are extremely serious, and make it imperative that the Commission strive to recommend a rate for E-COM that covers the service's long-run incremental cost. Indeed, these concerns were expressly recognized by the Commission in its Opinion and Recommended Decision in Docket No. MC78-3.

76/ Tr. 16/5175 (Owen).

77/ It is revealing that no Postal Service witness, including Dr. Willig, disputed the anticompetitive effect of cross-subsidization and below-cost pricing by the Postal Service.

[A] monopolist, by virtue of its market power, is under a special obligation to enter new markets on terms that will guard against cross-subsidization of the monopolist's penetration of a new market through monopoly profits earned in the monopolized market. Such safeguards are doubly important where the monopolist is authorized to determine the scope of its monopoly in its own interest, as the Postal Service is authorized to interpret the Private Express Statutes. . . . These considerations make imperative the careful consideration of system designs that allow competition in the non-delivery portions of electronic mail service.

Op. MC78-3 at 232-33. The Commission's conclusions remain as relevant today as they were in 1979.

C. Nothing In The Record Justifies E-COM Rates at Other Than Long-Run Incremental Cost

The discussion above demonstrates the adverse consequences of departing from the long-run incremental cost standard in recommending rates for E-COM. However, there are situations in which efficient pricing principles must give way to other considerations, and a departure from marginal cost pricing may be warranted. The record demonstrates that none of these justifications applies to E-COM.

1. The Record Does Not Demonstrate That E-COM Exhibits Economies Of Scale Or Economies Of Scope

Marginal cost pricing will not, in some circumstances, provide sufficient revenue to cover total costs. The first and most important circumstance is that of the so-called

The record contains substantial additional evidence of competition for E-COM. For example, witness Bernheimer testified concerning the operational and product similarities between E-COM and MASA members. Tr. 15/4360-64, 4511, 4646. (Bernheimer). As he stated: "E-COM is directly competitive with the business of MASA members." Tr. 15/4367 Thus, for the message processing components of E-COM service, E-COM does (and will in the future if priced to reflect all of its costs) face significant competition.

B. Recommending the E-COM Rates Proposed by the Postal Service Will Likely Result in the De Facto Extension of the Postal Monopoly into an Area where Congress has Expressly Refused to Extend Private Express Protection

The record leaves little doubt that the below-cost E-COM rates proposed by the Postal Service could eliminate or impair existing competition and deter private firms from entering the market for message processing and electronic mail services. If the Postal Service continues to price E-COM below cost, it will likely monopolize some or all of the message processing industry by driving out of business the letter shops, and by causing individual mailers to disintegrate their operations. Tr. 16/5168-69 (Owen). Dr. Owen testified that:

If you price below cost, and if you're in a position to do so indefinitely, you can monopolize the market whatever the size of it. You don't need to measure it to reach that conclusion. It's perfectly obvious. Pricing below cost a service which competes with other services, when the firm which is pricing below cost, has available to it an indefinite, permanent source for cross subsidy to finance

that below cost pricing, obviously it's capable of permanently monopolizing whatever the market is.

Tr. 17/5458-59. Indeed, Dr. Willig testified that:

Cross-subsidization becomes a pertinent possibility when a multi-product firm operates in a protected market in which it has some monopoly power or competitive advantage and in addition operates in other markets. Such a firm could, in such a setting, use revenues from its protected market to subsidize its other offerings and price its products in the other markets below costs.

USPS-RT-5 at 12. He confirmed that cross-subsidization can be "unfair" to consumers of the product in the protected market [First-Class Mail] and to competitors of the subsidized product [E-COM] because the subsidized price may be so low as to make entry into the market unattractive or continued production impossible. Id. Therefore, as Dr. Owen demonstrated, there can be no serious doubt as to the likely competitive effect of such a pricing scenario. Tr. 16/5169-74, 5458-59 (Owen).

Perhaps the most striking evidence supporting this conclusion is the testimony submitted by MASA, which represents a portion of the message processing industry directly threatened by E-COM. Mr. Bernheimer stated unambiguously that "MASA members cannot easily compete with E-COM in the long run in its market segment because they cannot match its price." Tr. 15/4367, 4646 (Bernheimer).

Moreover, considering the sequence of functions constituting electronic mail service, it is not entirely clear how far the leverage created by the Postal Service's market

power over First-Class Mail delivery extends. The Commission itself has recognized that if the Postal Service had exclusive control over, for example, site preparation or acceptance of messages which would give it a significant edge in the electronic mail market, "performance of those functions [would] constitute an extension of its monopoly over the delivery of letter mail." 134/ The ultimate effect of the below-cost rates proposed by the Postal Service will likely be the same. Driving rivals out of the market and monopolizing the message processing industry would, in effect, constitute an unauthorized extension of its monopoly over the delivery of letter mail.

134/ See Op. MC78-3 at 234-35.

APPENDIX B

Selected Utility Supply and Installation
Programs with Competition Problems

May 1984

1. One Northeastern utility proposed a solar water heater program in 1980 without the benefit of a public hearing. The utility asked for a waiver of the Federal prohibition against supply and installation (section 216(a) of the National Energy Conservation Policy Act) to allow six contractors exclusive rights in six territories (encompassing over one million customers) to sell solar water heaters backed by the utility. The proposed program was limited to only one brand of solar water heater, one with an electric back-up system. Thus, the utility was foreclosing the market to competing contractors and competing brands and types of solar water heaters. After much contractor protest, a public hearing was held, and the waiver was not pursued by the utility.

2. Another utility requested a waiver of the Federal prohibition to expand its appliance and energy conservation sales program to include storm doors and energy saving doors. Initially, it claimed a net profit of 12 percent of revenue.

After further inquiry by my office, the utility admitted that the program lost \$40 for every \$100 of sales for the last several years. Although we are told that the stockholders have been paying for these losses, the ratepayers may be asked in the future to subsidize these losses to the detriment of competing small businesses. If a hearing had been held at the state level, these facts could have been revealed, and thus the waiver would have been subject to proper scrutiny. At such a hearing, the better solution of using unregulated private firms to supply and install, at virtually no cost to the utility, could have been offered. This waiver is still pending.

3. Another utility requested a waiver stating there would be no ratepayer subsidy of its proposed activity. However, this same utility was the subject of a public utility commission proceeding that resulted in an adjustment of the utility's accounting procedures to eliminate an apparent cross-subsidy. However, without a local hearing, this fact was not explored. This waiver was, however, denied by the Department of Energy on other technical grounds.

4. At least five utilities with "grandfather" status⁵ have been the subject of numerous contractor complaints. Such complaints include unfair distribution of utility leads to contractors, and forcing subcontractors to use specified conservation materials. One "grandfathered" utility program was reported to have nearly the lowest consumer ratings in quality and cost in comparison to its local small business competitors.

5. Florida Power and Light's supply and installation program, the Florida Energy Store, is subsidized directly by ratepayers. The utility reports that it costs \$28 to process every \$15 order. The public utility commission ordered a hearing upon the request of a Florida contractor. As a result, Florida Power and Light recently offered to terminate the program instead of proceeding with the hearing.

6. Another utility offers a 30 gallon water heater for \$149, including free gas and plumbing installation, which, we are told, is less than the wholesale price of this product.

⁵These utilities are not subject to the general utility prohibition against supply and installation of section 216(a) of the National Energy Conservation Policy Act.

7. Other utilities offer rebates to customers who switch from competing fuels to their own fuel (e.g., oil to gas). These rebates are subsidized using ratepayer funds. Ratepayer money should not be used draw customers from competing fuel suppliers. Such expenditures hurt competing small business fuel suppliers (e.g., oil, propane) and suppliers and installers of related equipment.

8. In contrast, in California, there is an example of utility program for which state required a public hearing and significant competition concerns were addressed. Santa Monica's municipally-owned utility contracted out to install no-cost/low-cost conservation measures throughout the city. Through the involvement of small businesses at the hearing, the competition impact was limited through the adoption of a competitive bidding system and the specification of the low-cost/no-cost items to be installed. A public hearing process, particularly if early consultation with affected parties is included, can assuage much of the adverse competitive impact of utility supply and installation programs.

Mr. LUKEN. Mr. Swain, assuming for the moment agreement with the proposition that you advance that the utilities should not be allowed to compete in this unregulated area, are you suggesting that in order to accomplish this, it would be a State responsibility, not a Federal legislative responsibility?

Mr. SWAIN. The regulation of public utilities has traditionally been a State responsibility, and we are not advancing the proposition that the Federal Government ought to get in and regulate to any great extent in this area.

Mr. LUKEN. We are already in there, aren't we, with the Department of Energy? And you are the Federal Government, I believe.

Mr. SWAIN. To the extent that the CACS and the RCS statutes raise issues that the Federal Government is telling us to do this or the Federal Government is telling us to do that, I do think it's appropriate for the Federal statutes to be fine-tuned to clear up any of the problems that have been raised by these laws, but I don't think that we are talking about an overall regulatory scheme. That's still left in the hands of the States.

Mr. LUKEN. OK. Let's put aside an overall regulatory scheme, but with regard to the CACS—the Commercial and Apartment Conservation Service—program, would you recommend any change in that legislation?

Mr. SWAIN. Personally, I would recommend that, to the extent that that legislation now does not have a prohibition on utilities providing supply and installation services, as the RCS program does, that that specific defect be remedied so that utilities could continue in the energy audit business, they could continue in the referral business, they could continue, if they felt it was appropriate to their corporate goals, in the various types of financing schemes, but as far as the actual utility supply and installation of various conservation devices or systems, that that would remain a separate industry—not a utility industry but an energy industry allowed to develop on its own separate market path.

Mr. LUKEN. How far does this prohibition go in the RCS program? It prohibits utilities from becoming involved when the RCS program is invoked.

Mr. SWAIN. That's right; that's my understanding.

Mr. LUKEN. What percentage of repairs or renovations do you think that involves?

Mr. SWAIN. I wouldn't want to speculate without checking.

Mr. LUKEN. Something less than 100 of course?

Mr. SWAIN. Something less than 100.

It probably varies area by area, depending on the activity of the local utilities. We have heard a lot from small business people in the Northeast.

Mr. LUKEN. It's small, isn't it?

Mr. SWAIN. Depending on the area. The people we have heard from in the New York City area think it is a fairly significant problem in that area. It may not be at all a problem in Ohio, if we haven't heard from people in Ohio.

Mr. LUKEN. Does anyone have any information on that?

Mr. SABBATH. No, sir.

Mr. LUKEN. All right.

In the report issued by your office and in the Senate testimony, it is suggested that the DOE and the FTC provide written guidelines for States regarding small business and competition. Have in fact any guidelines been prepared?

Mr. SWAIN. I'll let the gentleman from the Federal Trade Commission speak to that issue.

We have, in preparing our report to the States, consulted both with the Federal Trade Commission and the Department of Energy, and we are advised informally that they had no objection or no disagreement with the recommendations that we gave to the States.

I can't answer for the Department of Energy.

We are aware of the fact that the Federal Trade Commission does have some activity ongoing in that area, and I'm sure that the witness from the FTC will—

Mr. LUKEN. You don't know whether they have really gotten any effective guidelines out there?

Mr. SWAIN. I do not believe that as of this afternoon there are formal guidelines that have been released by the Federal Trade Commission or the Department of Energy.

Mr. LUKEN. Well, the public utility commissions of the States have the authority to examine the issue of competition, do they not?

Mr. SWAIN. That's right.

Mr. LUKEN. You say they have not. Do you know why they have not?

Mr. SWAIN. I can speculate, and we have received some indications that some take the position that they do not have authority, that their authority is limited to being concerned about the ratepayer—the person that pays for the power—and that anything else is somewhat irrelevant.

Mr. LUKEN. Do they disagree with that conclusion that they have that authority?

Mr. SWAIN. Under specific State laws, some public utility regulatory boards take a narrow reading of the State laws. Others admit that they have the authority but claim that they have a tremendous workload and this just doesn't rank high on their priority lists.

But I am impressed by the fact that, having sent out our report—and it has been out for about 6 weeks now—as I indicated, generally we have received very positive feedback. In fact, a couple of the State agencies have written back to us and said, "We would like to hear more from small businesses on these particular sets of issues."

So again, I think that our reaction that we have gotten from the State public utility commissioners has been, "Gee, this is interesting; we haven't really thought it through before, and we want to learn more about it."

Mr. LUKEN. In your report, which is entitled "Utility Competition with Small Businesses"—that's the March 1984, report—and again in your statement here today, you say that utilities should not be competing in unregulated markets "unless there are very substantial benefits that outweigh anticompetitive dangers."

How would you define those? Would you ban the utilities that are engaged in these endeavors which predated the residential conservation and the CACS audit requirements?

Mr. SWAIN. Of course the Federal laws take the position, predating the various Federal statutes, utility activities are grandfathered in, and I think that in that case, that's a tough call.

Mr. LUKEN. Who takes that position?

Mr. SWAIN. The Federal statute now allows certain utilities to engage in supply and installation services.

Mr. LUKEN. That's the RCS and the CACS?

Mr. SWAIN. Yes, because they were involved in those activities before the enactment of those two laws, and so those utilities are, in effect, grandfathered.

Mr. LUKEN. As far as those statutes are concerned?

Mr. SWAIN. That's right. In general, we think that the best of all possible worlds is that the utilities do what they do best, which is generate and supply power at the lowest possible cost to the consumers, and that the energy market—the energy conservation market do what it does best, which is supply and make technological innovations in the energy conservation area. The potential for cross-subsidization is tremendous, and therefore, in the best of all possible worlds we would be prefer not to allow the opportunity for utilities at all in the energy market.

The second best is, if utilities are in the supply and installation business, at the very least, there should be full public disclosure of the methods in which they are in those businesses, and the finances to make sure that there are not any potential improper competitive situations.

Mr. LUKEN. You state that there are certain types of public benefits which might justify utilities entering these markets. I wonder what kind of public benefits would be a justification.

Mr. SWAIN. You are basically asking me to speculate what the worst of all cases for small business is that you would allow a utility to get in, and I guess I would be tempted to say that if a utility could prove that there was no alternative to supply and installation of energy conservation but for the utility to supply it, then that would be a legitimate reason to allow a utility to do something that no one else in the business community could do. But, of course, I don't believe that's the situation at all. There is no section of the country where there is not a very capable, and active, and technologically sophisticated small business community that can supply energy conservation services.

So I would be hard pressed to define a public benefit that was so important that it would allow utilities into this particular type of business when they are not in it right now and when the Federal policy is against getting them into it.

Mr. LUKEN. Well, in view of that answer then, I don't think you would agree that the energy crisis, in itself, as we have known it would be a sufficient kind of a reason for such suspension.

Mr. SWAIN. I think the energy crisis is a tremendously important reason to have energy conservation in general, but I see no reason why an energy crisis would lead to saying that the utilities are the best ways of providing those energy conservation measures.

Mr. LUKEN. I think you have done, a good job of laying out some groundwork here. That's all the questions that I have.

Mr. Gonzalez?

Mr. GONZALEZ. Thank you, Mr. Chairman. You have covered the ground, and I think the witness gave very good testimony.

Mr. SWAIN. Thank you, Mr. Gonzalez.

Mr. LUKEN. All right. You are excused, Mr. Swain, and we thank you very much.

The next witness is Sid Moore, who is an Assistant Director of the Bureau of Competition for the Federal Trade Commission.

Mr. Moore, I believe we have some written testimony from you, which will be received into the record, without objection. You may proceed.

**TESTIMONY OF WINSTON S. MOORE, ASSISTANT DIRECTOR,
BUREAU OF COMPETITION, FEDERAL TRADE COMMISSION**

Mr. MOORE. Thank you, Mr. Chairman.

My statement is relatively short. I think I will summarize it and read a few excerpts from it, sir.

I am pleased to participate today in your consideration of this important issue.

The diversification of regulated utilities into unregulated markets raises significant concerns about competition, particularly the effect of this phenomenon on the ability of certain small firms to survive. In addition, utility diversification can affect utility rates as well as the supply and price of other goods and services available to consumers.

I should note that my remarks today are on behalf of the staff of the Federal Trade Commission; I do not speak for the Commission itself or for any individual commissioner.

I plan to focus my comments today on four areas. The first consists simply of an overview of how we at the FTC see this issue and the potential competitive problems that may arise in connection with utility diversification.

The second concerns the role the FTC may play in this arena, within the bounds of our statutory authority.

The third area relates to our activity in examining this issue to date.

Fourth and finally, I will briefly mention some preliminary findings resulting from our study of the matter.

Let me now turn to the first point: The principal goal of the FTC is to serve the interests of consumers of goods and services in the United States. We attempt to achieve this goal primarily through enforcement of antitrust and consumer protection laws as well as through the provision of advice to other Government agencies on how to fulfill their respective policy objectives in a manner consistent with the interests of consumers and the value of open competition.

Accordingly, our historical interest in small business stems primarily from the very significant contribution small businesses make to vigorous competition, which in turn leads to the most efficient combination of output and price for the goods and services consumers want.

In general, the entry of additional competitors into a market will enhance free and open competition. If a new entrant has some characteristic which enables it to provide a good or service to consumers at lower cost, then this particularly helps consumers and the economy in general.

Thus, it ordinarily is no service to consumers or to the health of the American economy to stand in the way of a new, low-cost supplier in order to ensure the continued existence of higher cost suppliers, whether they be small businesses or large.

However, if a new entrant possesses a competitive advantage which is not based on its being more efficient—for example, if it can subsidize its new business with revenues from a Government-sanctioned monopoly—then consumers and efficient competitors will suffer.

A regulated utility might be able to do this by charging costs to its regulated business which are properly attributable to its unregulated business.

If the appropriate regulatory commission acquiesces in this accounting treatment, then the utility's approved rates will be set sufficiently high to recover these costs from the utility's ratepayers.

So-called cross-subsidization can result in a misallocation and waste of society's resources. For example, a utility's cross-subsidization of the sale of new appliances may induce people to purchase new replacement appliances at artificially low prices in situations where it may be more efficient for the consumer to obtain repairs for older appliances.

In an extreme case, this activity could violate the antitrust laws. If cross-subsidy were carried out to the extent that the utility was able to set its prices in the unregulated market below its actual costs, then it might be able, first, to drive from the market even the most efficient competitors that lacked the ability to cross-subsidize, and then to raise its prices and obtain monopoly profits.

This conduct, if successful, would constitute a violation of the Sherman Act and could form the basis for an FTC challenge to the utility.

Another, probably larger, category of situations appropriate for FTC action are those in which a cross-subsidy or other anticompetitive practice exists but the utility's behavior does not rise to the level of an antitrust violation.

On prior occasions, consistent with our role as an advocate for competition and consumers, we have appeared before the Congress or a State legislature, or a Federal or State regulatory body, to call attention to practices that may injure competition and consumers.

Under this approach, we could, and quite likely will, intervene in a ratemaking proceeding before a State regulatory commission, for example, and point out the harm to competition, consumers, and small business that could result from allowing a cross-subsidy to occur.

Attorneys from the FTC's Bureau of Competition and economists from the Bureau of Economics are collaborating on related efforts to examine this issue.

Since last fall, we have been working closely with representatives of the trade associations from the various industries potential-

ly affected by utility diversification to examine complaints from different types of businesses in different parts of the country.

In this regard, the staff has looked into hundreds of reports of utility competition in unregulated markets, including about 30 direct complaints from small businessmen. The matters we have evaluated involve about 75 utilities in approximately 40 States.

As a result of this process, the Bureau of Competition has now focused on several specific instances of possible anticompetitive activities by diversified utilities and other parties.

We will conduct a complete, in-depth review of the facts in these situations to determine the significance of applicable State laws, the views of State officials, the best way to handle an evaluation of the utilities' accounting data, and, ultimately, what FTC action is appropriate under the circumstances.

Although there is still much to be done before we can draw clear conclusions, the information we have studied suggests four points I will share with you.

First, some of the problems are likely to be a matter of the utilities having cost advantages that would not create antitrust liability even if such advantages were thought to be obtained through cross-subsidies.

For example, if a utility must maintain a fleet of vehicles or a group of workers in order to carry out its utility operations, the antitrust laws do not prohibit the utility from seeking more efficient use of resources by using those trucks or workers in some other business during slack periods, provided, of course, that all avoidable costs were charged to the unregulated business.

In such cases, the utility's use of such resources in an ancillary business would not affect its rates, because the firm would still have to pay for the trucks and workers even if it were not involved in the ancillary business.

A utility's opportunity to achieve this type of savings may have various results from a policy perspective. On the one hand, independent firms may face tougher competition in their markets. On the other hand, consumers would benefit from the cost savings and lower prices derived from putting these assets to more efficient use.

Second, we have found indications that diversified utilities very often have small market shares in the ancillary markets they have entered.

To the extent that utilities have an unfair competitive advantage in these markets, we would expect to see them acquire a significant share of the market from the established competitors.

Thus, at least based on the developments to date, the actual effect of utility diversification in many cases may not be as great as some competitors of the utilities have feared. Alternatively, this may indicate that we are observing this phenomenon of utility diversification at a very early stage of its development.

Third, some situations that at first glance seem to present examples of a utility's unfair advantage may turn out to be examples where the utility is able to avoid anticompetitive and unjustified regulatory requirements that previously benefited only a limited group of established competitors.

For example, we looked into a complaint that a utility uses maintenance personnel to install water heaters under the supervision of a licensed master plumber.

The master plumbers complained that the utility's use of maintenance personnel was unfair because it permitted the utility to offer the service at a lower price, but it may well be that a master plumber's license is not really an essential qualification for the actual installation work and that valid safety concerns would be met by having the unlicensed installers supervised by a master plumber.

If so, a regulation requiring all work to be done by master plumbers would injure consumers and also work to the disadvantage of numerous small plumbing businesses who otherwise could compete with the utility by installing water heaters at lower cost.

The fourth point is similar—

Mr. LUKEN. That issue with reference to using utility employees or using nonprofessional employees—

Mr. MOORE. The point there I was making concerned the use of nonprofessional employees.

Mr. LUKEN. Was that the basis of the complaint?

Mr. MOORE. Yes.

Mr. LUKEN. It seems to me there would still be an issue whether there are not—there are two issues. You have addressed the one. The master plumber issue.

Mr. MOORE. The other issue is similar to what I was talking about earlier in terms of the trucks.

If a utility, for peak load reasons, or to deal with problems caused by storms, or whatever reason, has to have these workers on its payroll, it makes sense—from a cost saving to both the utility and the consumer—to assign those workers other chores when they otherwise would be idle, provided that all the variable costs of that extra activity are not charged back to the ratepayer.

That is, simply, if those trucks and people have to sit idle, waiting for the hurricane to come, those resources are wasted in a sense. If they could be put to use, that is a more efficient way of getting some of these services to the consumer.

Exactly how the costs are to be allocated is difficult question in terms of the utility commission trying to determine exactly where these costs should be allocated, but public utility commissions have been doing this for years. They have had a long experience with the telephone industry for example.

Mr. LUKEN. We are going to grandfather it in because they have been doing it for years?

Mr. MOORE. No; Mr. Chairman, my point is that the utility commissions have had to try to make these decisions on cost allocation for years.

The fourth point is similar. Well intentioned governmental actions may be responsible for some cross-subsidy situations because competitive impact was not taken into account.

For example, we have received complaints on behalf of campground operators in the State of Oregon that utilities are offering camping services at unjustifiably low prices. The utilities apparently operate campgrounds on land they own in connection with dams built for hydroelectric power generation projects.

When we investigated, we learned that the basic facts were true, but the utilities are merely adhering to a requirement imposed by the Federal Energy Regulatory Commission in conjunction with the licensing of the power project.

The FERC, of course, regarded the low prices as a public service. At the same time, however, the requirements may damage competition and small campground operators.

In sum, the FTC staff shares this committee's concern about the competitive difficulties certain small businesses are facing and possible antitrust violations or regulatory imperfections associated with utility diversification.

We have acted based on this concern by assigning lawyers and economists to analyze specific complaints we have received, to perform in-depth studies, and to conduct empirical economic research.

We plan to continue the work we have started and to follow up as necessary in those situations where it seems appropriate.

We look forward to continuing to work with you and other groups interested in this issue.

Thank you for providing this opportunity for us to express our views. I would be pleased to address any questions the members of the subcommittee may have.

[Mr. Moore's prepared statement follows:]

PREPARED STATEMENT OF WINSTON S. MOORE, ASSISTANT DIRECTOR, BUREAU OF
COMPETITION, FEDERAL TRADE COMMISSION

I am pleased to participate today in your consideration of this important issue. The diversification of regulated utilities into unregulated markets raises significant concerns relating to competition in the unregulated markets, particularly the effect of this phenomenon on the ability of certain small firms to survive. In addition, utility diversification could affect utility rates, as well as the supply and price of other goods and services available to consumers. I should note that my remarks are on behalf of the staff of the Federal Trade Commission, and I do not speak for the Federal Trade Commission itself, or for any individual Commissioner.

I plan to focus my comments today generally on how the Federal Trade Commission fits into governmental treatment of this issue. Specifically, I will address four areas. The first area consists simply of an overview of how we see this issue and the potential competitive problems that may arise in connection with utility diversification. The second concerns the role the FTC may play in this arena, within the bounds of our statutory authority. The third area relates to our activity in examining this issue to date. Fourth, and finally, I will briefly mention some preliminary and tentative findings resulting from our study of the matter. Let me turn now to the first point.

OVERVIEW OF THE COMPETITION ISSUES

The principal goal of the FTC is to serve the interests of consumers of goods and services in the United States. We attempt to achieve this goal primarily through enforcement of antitrust and consumer protection laws, as well as through the provision of advice to other governmental entities on how to fulfill their respective policy objectives in a manner consistent with the interests of consumers and the values of open competition. Accordingly, our historical interest in small business stems from the very significant contribution small businesses make to the vigorous competition, which in turn leads to the most efficient combination of output and price for the goods and services consumers want. In general, the entry of additional competitors into a market will enhance free and open competition. If a new entrant has some characteristics which enables it to provide a good or service to consumers at lower cost, then this particularly helps consumers. Thus, it ordinarily is no service to consumers or to the health of the American economy to stand in the way of a new, low-cost supplier in order to ensure the continued existence of higher-cost suppliers, whether they be small businesses or large.

Having laid out this general framework, let us focus more narrowly on the kind of situation that could be at odds with these principles. If a new entrant possesses a competitive advantage which is not based on its being more efficient—for example, if it can subsidize its new business with revenues from a government-sanctioned monopoly—then consumers and efficient competitors will suffer. A regulated utility might be able to do this by charging costs to its regulated business which are properly attributable to its unregulated business. If the appropriate regulatory commission approves of or acquiesces in this accounting treatment, then the utility's approved rates will be set sufficiently high to recover these costs from the utility's ratepayers.

So called "cross-subsidization" can result in a misallocation and waste of society's resources. For example, a utility's cross-subsidization of the sale of new appliances (i.e., the sale of appliances below cost) may induce people to purchase new, replacement appliances at artificially low prices in situations where (based on actual costs) it may be more efficient for the consumer to obtain repairs for older appliances.

In an extreme case, this activity could violate the antitrust laws. If cross-subsidization were carried out to the extent that the utility was able to set its prices in the unregulated market below its actual costs, then it might be able first to drive from the market even the most efficient competitors that lacked the ability to cross-subsidize, and then to raise its prices and obtain monopoly profits. This conduct, if successful, would constitute a violation of the Sherman Act and could form the basis for an FTC challenge to the utility.

POSSIBLE FTC ACTIVITY IN THIS AREA

The FTC has two possible courses of action available to it to attempt to remedy consumer injury caused in the event cross-subsidization is found to exist. The first, of course, is an antitrust enforcement proceeding where there is evidence of predatory pricing by a utility. This approach requires the favorable resolution of a number of difficult legal issues. First, we would have to prove that cross-subsidization not only exists, but is occurring to a sufficient degree to enable the utility to price below its costs in the unregulated market. Given the massive volume and complexity of the accounting data maintained by large utilities, this is likely to be a monumental task.

Second, we must show that the unregulated industry is characterized by substantial barriers to entry, in order to insure that predatory conduct by the utility would be detrimental to competition in the long run. In other words, if the utility drove out other sellers of heating and cooling equipment, for example, we would need to show that it would be difficult for those or other firms to re-enter if the utility later raised its prices above competitive levels. Most of those unregulated markets appear, on the basis of what we know so far, to have relatively low entry barriers.

Third, we must be cognizant of the state action defense afforded under the antitrust laws. As articulated by the U.S. Supreme Court in *Parker v. Brown*, 317 U.S. 341 (1943), and several later cases, this doctrine shields from the antitrust laws certain conduct that is the express policy of a state. Thus, a utility might argue that if a state regulatory commission, under the authority of a state statute, affirmatively orders and actively supervises a cross-subsidy, then it may be immune to FTC attack, even if the utility's conduct would otherwise violate the antitrust laws. Notwithstanding these difficulties, we remain alert to the potential problem and, as I will discuss below, are actively looking into possible antitrust violations by diversified utilities.

Another, probably larger, category of situations appropriate for FTC action are those in which a cross-subsidy or other anticompetitive practice exists, but the utility's behavior does not rise to the level of an antitrust violation. On prior occasions, consistent with our role as an advocate for competition and consumers, we have appeared before the Congress or a state legislature, or a federal or state regulatory body, to call attention to practices that may injure competition and consumers. Under this approach, we could, and quite likely will, intervene in a rate-making proceeding before a state regulatory commission, for example, and point out the harm to competition, consumers and small business that could result from allowing a cross-subsidy to occur.

I would like now to move from the general to the specific, and tell you about what we have been doing in this area over the past few months.

FTC ACTIVITY RELATING TO UTILITY DIVERSIFICATION

Attorneys from the FTC's Bureau of Competition and economists from the Bureau of Economics are collaborating on two related efforts to examine this issue. Since

last fall, we have been working closely with representatives of trade associations from the various industries potentially affected by utility diversification to examine complaints from different types of businesses in different parts of the country. Our objective has been to identify those situations constituting the most likely sources of a significant competitive problem. At the same time, we have been hoping to find situations representing as many different categories of complaints as possible, so as to learn as much as possible from our follow-up efforts. In this regard, the staff has looked into hundreds of reports of utility competition in unregulated markets, including about 30 direct complaints from small businessmen; interviewed approximately 50 representatives of businesses, trade groups, utilities, and government agencies; and retained the services of an outside expert on public utility regulation. The matters we have evaluated involve about 75 utilities in approximately 40 states.

As a result of this process, the Bureau of Competition has now focused on several specific instances of possibly anticompetitive activities by diversified utilities and other parties. We will conduct a complete, in-depth review of the facts in these situations to determine the significance of applicable state laws, the views of state officials, the best way to handle an evaluation of the utilities' accounting data, and, ultimately, what FTC action is appropriate under the circumstances. Perhaps equally important, what we learn and do in these investigations may serve as a model for treatment of other, similar complaints we receive.

Simultaneously, the staff is pursuing an empirical economic study of diversified utilities, particularly the relationship between diversification and the level of rates. Systematically higher rates charged by utilities competing in unregulated markets could constitute evidence of a widespread competitive problem resulting from utility diversification. To date, the economists in our Bureau of Economics have completed several phases of this project, and the remaining work should be finished in the next few months.

SOME GENERAL OBSERVATIONS

Although there is still much to be done before we can draw clear conclusions, the information we have studied preliminarily suggests four points I will share with you. First, some of the ostensible competitive problems are likely to be a matter of the utilities having cost advantages that would not create antitrust liability even if such advantages were thought to be obtained through cross-subsidies. For example, if a utility must maintain a fleet of vehicles or a group of workers in order to carry out its utility operations, the antitrust laws do not prohibit the utility from seeking more efficient use of resources by using those trucks or workers in some other business during slack periods (provided, of course, that all avoidable costs were charged to the unregulated business). In such cases, the utility's use of such resources in an ancillary business would not affect its rates, because the firm would still have to pay for the trucks and workers even if it were not involved in the ancillary business.¹ A utility's opportunity to achieve this type of savings may have various results from a policy perspective. On one hand, independent firms may face tougher competition in their markets; on the other hand, consumers would benefit from the cost savings (and lower prices) derived from putting these assets to more efficient use.

Second, we have found indications that diversified utilities very often have very small market shares in the ancillary markets they have entered.² If and to the extent that utilities have unfair competitive advantages in these markets, we would expect to see them acquire a significant share of the market from the established competitors. Thus, at least based on the developments to date, the actual effect of utility diversification in many cases may not be as great as some competitors of the utilities have feared. Alternatively, this may indicate that we are observing the phenomenon of utility diversification at an early stage of development. The apparent lack of entry barriers in many of these ancillary markets also tends to preclude accumulation of large market shares.

Third, some situations that, at first glance, seem to present examples of a utility's unfair advantage may turn out to be examples where the utility is able to avoid

¹ Of course, if the utility purchased additional trucks or hired additional workers—solely for the unregulated business—and incorporated these additional costs into its utility rates, then this would warrant corrective action on the part of the public utility commissions concerned or perhaps the state and federal agencies charged with protecting consumers and competition.

² The use of the term "market" here does not necessarily mean "market" in the sense used for antitrust analysis. For example, a firm's volume of home insulation sales could account for different market shares, depending on whether the relevant market were deemed to include all insulation, all energy conservation devices, or even all energy sources.

anticompetitive and unjustified regulatory requirements that previously benefited only a limited group of established competitors, to the detriment of consumers. For example, we looked into a complaint that a utility uses maintenance personnel to install water heaters under the supervision of a licensed master plumber. The master plumbers complained that the utility's use of maintenance personnel was unfair because it permitted the utility to offer the service at a lower price. But it may well be that a master plumber's license is not really an essential qualification for the actual installation work and that valid safety concerns would be met by having the unlicensed installers supervised by master plumbers. If so, a regulation requiring all work to be done by master plumbers would injure consumers and also work to the disadvantage of numerous small plumbing businesses, who otherwise could compete with the utility by installing water heaters with lower-cost labor.

The fourth point is similar: well-intended governmental actions may be responsible for some cross-subsidy situations because the competitive impact was not given sufficient attention or weight. For example, we received complaints on behalf of campground operators in the state of Oregon that utilities are offering camping services at unjustifiably low prices. The utilities apparently operate campgrounds on land they own in connection with dams built for hydro-electric power generation projects. When we investigated, we learned that the basic facts were true, but that the utilities are merely adhering to requirements that had been imposed by the Federal Energy Regulatory Commission ("FERC") in conjunction with the licensing of the project. The FERC, of course, regarded the very low prices as a public service. At the same time, however, the requirement may damage competition among private campground operators.

CONCLUSION

In sum, the FTC staff shares this committee's concern about the competitive difficulties certain small businesses are facing and possible antitrust violations or regulatory imperfections associated with utility diversification. We have acted based on this concern by assigning lawyers and economists to analyze specific complaints we have received, perform in-depth studies of certain situations, and conduct empirical economic research into the problem. We plan to continue the work we have started, and to follow up as necessary in those situations where it seems appropriate. We look forward to continuing to work with you and other groups interested in this issue. Thank you for providing this opportunity for us to express our views. This completed my prepared testimony. I would be pleased to address any questions the members of the subcommittee may have.

Mr. LUKEN. Mr. Gonzalez.

Mr. GONZALEZ. Here again, you say you have a study underway?

Mr. MOORE. Yes, sir.

Mr. GONZALEZ. And how many States did you say you were surveying?

Mr. MOORE. We surveyed over 40 States, and essentially what we have been doing is looking for the most serious problem. Frankly, with respect to the grandfathering issue, the more serious problems from a competitive perspective seem to be associated, in our view at this point, with companies that were in the business before conservation acts such as NECPA were passed in the late 1970's.

Mr. GONZALEZ. I can see that from my own State as an example.

I am sure you have various State abilities to regulate through their State utility commissions.

Mr. MOORE. There is, of course, a great deal of variation, although the model is fairly standard.

Essentially, what we would do, in a case where we found that there was a particularly serious problem, would be first to consult with the State utility commission, perhaps jawbone the State utility commission to permit us to participate formally in a rate case in order to point out the competitive problems. That is, I think, consistent with cooperative federalism, and we contemplate taking that sort of first step in appropriate cases.

Mr. GONZALEZ. So that actually, though, from the FTC standpoint, you are looking at it from enforcement from the anti-Sherman—

Mr. MOORE. Sherman, Clayton, and FTC acts primarily.

Mr. GONZALEZ. Thank you very much, sir. I appreciate your statement.

Mr. LUKEN. Mr. Muris is your boss, isn't he?

Mr. MOORE. That's correct.

Mr. LUKEN. He stated in Senate testimony that bill stuffing by utilities and charging for unregulated services on the monthly bill—those two are not cross-subsidies because the billing must be done in any event. Is that the position of the FTC?

Mr. MOORE. It is not a cross-subsidy as long as the utility does not include the variable cost of the advertising insert in its rates.

Our view of the matter is that the utility would have to undergo 99 percent of the cost associated with sending the mailing in the first place, so I do not believe it is a cross-subsidy in the worst sense where the utility is transferring costs solely attributable to its unregulated business to the consumer of gas, electricity, or whatever.

However, if a State regulatory commission were to decide to allocate those costs between the unregulated and regulated businesses, I don't think the FTC would object. It may turn out to be 99 and 1, however, sir.

Mr. LUKEN. Is that what they are doing, prorating it?

Mr. MOORE. I have no information at this point on whether utilities are allocating these costs, but that is a conceivable and not an incorrect response.

Mr. LUKEN. Well, it certainly results in a tremendous advantage to the utility.

Mr. MOORE. It is an inherent advantage they have.

Mr. LUKEN. Because of the fact they are in a regulated monopoly business.

Mr. MOORE. It is, and because of economies of scale and scope associated with their size and the fact that they are in more than one line of business.

Mr. LUKEN. And they are big because they are in the regulated monopoly business.

Mr. MOORE. It is a competitive advantage. There are a number competitive advantages that the smaller concerns have, too; for example, they can change more quickly.

Mr. LUKEN. Now, some have argued that remedies are available to small business through private antitrust lawsuits. Would you agree with that? You say you don't think that's an antitrust violation.

Mr. MOORE. No, but let's stipulate that it might be. There is certainly a conceivable case in a situation where the utility bought trucks only to install water heaters and furnaces, put them in the rate base, and either got the State public utility commission to agree to it or, better from a legal perspective for the antitrust plaintiff, slipped it by the State public utility commission.

That kind of advantage certainly would raise a lot of competitive concerns and might present a case where the transferring of the costs of investment in the unregulated business, back to the regu-

lated business, back to the regulated business could violate the antitrust laws.

Mr. LUKEN. If a utility were to price significantly below the apparent marginal cost and yet the public utility commission reported no clear subsidy, would the FTC be inclined to examine the matter?

Mr. MOORE. Well, we would certainly persist in trying to get the public utility commission to reconsider the matter. These rate cases come up periodically, and a decision this year doesn't preclude a different decision the next year.

In terms of concerns of federalism, we would have to think long and hard before doing any more than that; but we would certainly think about it.

Mr. LUKEN. All right. Your testimony and the questioning has come to a happy coincidental conclusion at the same time as we are called to the floor, and I'm advised that we will have four different bills to vote on. That's not quite as foreboding as it may sound. It means that we will be gone for about 25 minutes.

Let us reconvene at 2:15. We will recess until that time.

[A short recess was taken.]

Mr. LUKEN. My apologies for the delay, but hopefully we will have an uninterrupted period of time now.

We would like to invite a panel to be the next witnesses: Dennis Lavallee of the Alliance for Fair Competition; Bill Greene of Central Roofing & Siding of Rockville, MD; Jim Johnson of Midway Supply in Seymour, IN; and Harold "Joe" Hagar, president of Farm & Gustafson Plumbing and Heating of Mankato, MN.

Who wants to lead off?

Mr. LAVALLEE. Dennis Lavallee.

Mr. LUKEN. Mr. Lavallee.

TESTIMONY OF DENNIS LAVALLEE, COCHAIRMAN, ALLIANCE FOR FAIR COMPETITION

Mr. LAVALLEE. Mr. Chairman, thank you for giving us this opportunity to call congressional attention to a grievous assault on small business.

My name is Dennis Lavallee. I am cochairman of the Alliance for Fair Competition. This is a coalition of 18 national groups who have banded together to combat what we view as unfair and anti-competitive practices by utilities.

This afternoon, you will hear from representatives from three of the groups who will provide illustrative examples of unfair competition from utilities. There are many, many more which could have been presented, and we have provided your staff with documentation on many of these.

Before they testify, I am going to provide a brief overview and answer some key questions about the issue of utility competition.

First, what's unfair about utility competition, and how is it different than competition from other businesses?

All of us, as small businesses, support fair and open competition. However, a utility company is given protected status. It is guaranteed the opportunity for a rate of return and given monopoly status. In exchange, it is regulated by the State regulatory commis-

sion. Its size and resources far outstrip many small businesses in the community.

When this protected entity is permitted to compete in other markets, there are market advantages which it can exploit unfairly.

Picture for a moment a fortress surrounded by fields. Men are competing on the field in hand-to-hand combat. Symbolizing small businesses, they are limited in resources. The fortress symbolizes the State regulatory commission which provides a protective enclosure for the garrison within. Here the utility can amass its resources and use them—food, fresh horses, weapons, whatever.

Then troops are sent forth to join the field combat. Clearly, they have a competitive advantage that they can critically injure, if not destroy, the combatants already there.

What is the nature of the resources that provides the utility with that market advantage? Cross-subsidization of energy audits is one notable example which is congressionally mandated.

In addition, we believe that the utility regulatory commissions are not effectively controlling ratepayer subsidization of a utility's indirect costs. Capitalization through loans, loan guarantees, or other financial subsidies to a new business entity; administration and overhead; use of the utility's name; credit information from the customer's bill payment records; billing; the postage, mailing, and personnel costs are already being paid by the ratepayers.

Advertising, for example the postage for a bill stuffer is paid by ratepayers as part of their utility bill; direct mail, through the use of the most up-to-date mailing lists in existence; market data; selective referral and market allocation, a utility can make or break a small business by arbitrarily referring or not referring business. That same market advantage can be of tremendous competitive value if the utility funnels the business to itself; and consumer financing.

The other witnesses this afternoon will provide examples of many of these marketing benefits which give the utility an unfair advantage.

Is this a new problem? In fact, the problem has been around for quite a number of years. Let me give you an historical overview.

A major root of the problem is the competition between fuel types, such as when the gas and the electric utilities each strive to maintain and increase their market share.

At least once before in recent history, this has produced a public outcry resulting in congressional attention. In 1968, Congressman John Dingell conducted hearings on utility promotional practices before his subcommittee here in the House.

In 1978, Congress passed legislation creating the Residential Conservation Service, which we have already discussed some this afternoon. This requires the utilities to offer and subsidize energy audits, a service already offered by many small businesses.

Although the legislation had provisions prohibiting utility supply and installation, numerous loopholes made those prohibitions virtually meaningless.

In 1980, Congress enhanced the problem by creating the Commercial and Apartment Conservation Service and failed to include even the weak anticompetitive protections which were included in the RCS program. Utilities will be free to offer not only audits to

our customers but also to use the in-home and in-the-business audits as marketing opportunities to promote their own supply, installation, and service programs.

To combat unfair competition problems, the Alliance for Fair Competition was formed. We have done a number of things, including encouraging the formation of local coalitions.

We have asked the FTC to investigate, and as you have heard this afternoon, they are pursuing this with a study.

We have provided the Senate Small Business Committee with information during hearings last November.

We have commented to the Small Business Administration during their preparation of their report on "Utility Competition With Small Business."

We have provided Congress with some suggested amendments for the RCS and CACS legislation.

The question came up earlier—and I'll repeat it here—isn't this a State issue? This is in fact, and we accept that this is in fact, a State issue for State public utility commissions.

However, unfair utility competition is also an issue for Federal public policy concern, particularly, one, when State commissions decline to consider the issue of competition or conclude that they do not have the authority over the unregulated activities; two, when utility practices violate the antitrust laws; three, when Congress requires utility activity; four, when utility activities cross State lines, preventing effective regulation by a State commission.

And how is the consumer affected? If utilities are permitted to control the market or to limit competition, consumer choice is reduced. The consumer would be better served if none of the unregulated activities are charged to the ratepayer.

If a bill stuffer goes with the utility bill, all of the costs for the bill stuffer—postage and mailing—should be charged to the unregulated activity. Such a proposal would lower utility rates.

Here are our recommendations from the coalition.

One, we fully support the Small Business Administration advocacy report, which recommends that utilities should be prohibited from sales, installation, or service.

Two, antitrust enforcement should be expedited before there is irreparable injury to competition.

Three, Congress should strengthen the antitrust laws to prohibit the abuse of marketing practices to compete in unregulated markets.

Four, Congress should amend the RCS and CACS programs to build in the strong anticompetitive protections necessary or repeal the programs.

Again, thank you for scheduling the hearings, and I believe that members of the coalition now will tell you problems that affect them in their communities.

[Mr. Lavalley's prepared statement follows:]

PREPARED STATEMENT OF DENNIS LAVALLEY, COCHAIRMAN, ALLIANCE FOR FAIR
COMPETITION

Mr. Chairman. Thank you for scheduling these hearings on competition with small business by utilities and for giving us an opportunity to call congressional attention to this grievous assault on small business.

My name is Dennis Lavalley and I am co-chairman of the Alliance for Fair Competition (AFC). This is a coalition of 18 national groups who have banded together to combat unfair and anticompetitive practices by utilities. Included in our numbers are three other coalitions (Associated Specialty Contractors, National Construction Industry Council, Small Business Legislative Council) who share our concern (See Attachment A). Together, we include 68 major trade organizations representing more than four million small businesses.

This afternoon, you will hear from representatives of three of the groups who will provide illustrative examples of unfair competition from utilities. There are many many more which could have been presented and we have provided your staff with documentation on them.

WHAT'S UNFAIR ABOUT UTILITY COMPETITION

So, why is competition from utilities any different than competition from other businesses?

Small businesses support fair and open competition. However, a utility company is given protected status. The utility is granted monopoly status (free from competition) and is guaranteed the opportunity for a rate of return. In exchange for this protected status, it is regulated by the state regulatory commission.

Usually a large business, its size and resources far outstrips many small businesses in the community. When this protected entity is permitted to compete in other markets, there are market advantages which it enjoys which are unmatched by most others, particularly small businesses.

Picture for a moment a fortress surrounded by fields. Men are competing on the field in hand to hand combat. Symbolizing small businesses, they are limited in resources. The fortress symbolizes the state regulatory commission which provides a protective enclosure for the garrison within. Here the utility can amass its resources and use them—food, fresh horses, weapons. Then, troops are sent forth to join the field combat. Clearly, they have a competitive advantage that can critically injure, if not destroy, the combatants already there.

What's the nature of the resources that provides a utility with that market advantage?

Cross-subsidization—While generally state regulatory commissions prohibit a utility from using its regulated activities to subsidize its unregulated activities, energy audits are one notable exception in which the utility is congressionally mandated to use ratepayer money to subsidize a business activity currently performed by small business. In addition, we believe that the commissions are not effectively controlling ratepayer subsidization of a utility indirect costs.

Capitalization—The utility may provide loans, loan guarantees, or other financial subsidies to a new business activity.

Administration and overhead—Management, planning, accounting, legal assistance, research and development resources may be used by a utility to start up or operate other lines of business. In addition, office space, equipment, or personnel of the utility may be available.

Name—Instant name recognition is a valuable asset which a utility enjoys when venturing into a new market.

Credit information—From customers' bill payment records, the utility has a built in source of credit information for use in other business activities.

Billing—Postage, mailing and personnel costs are already being paid by the ratepayers. Adding charges for other business activity to the bill produces very little expense to the other activity.

Advertising—In many states, advertising costs can be passed on to ratepayers. While advertising directly connected with an unregulated activity may need to be charged to that activity, there are many opportunities for the utility to also include material with advertising promoting its regulated activities. The postage for bill stuffers promoting a service contract is paid by ratepayers as part of their utility bill.

Direct mail—With utility bills going out monthly and with immediate access to customers initiating or terminating service, utilities have the most up-to-date mailing lists in existence.

Market data—To promote their fuel type, utilities frequently have extensive market data on their customers. This may readily be made available for marketing of its unregulated business activities.

Selective referral and market allocation—With its access to information on consumer needs and requests, a utility can make or break a small business by arbitrar-

ily referring or not referring business. That same market advantage can be of tremendous competitive value if the utility funnels the business to itself.

Direct from the manufacturer ordering—With larger volume orders, the utility can circumvent usual distribution channels, such as suppliers, contractors, and retailers, and buy direct from manufacturers with possible favorable pricing for bulk orders.

Consumer financing—The utility's large capital base gives utility access to providing favorable consumer financing. Financing may be added right on to the utility bill.

Consolidated tax returns—The utility may reap financial benefits from consolidating its financial data for tax purposes.

These are some of the more significant benefits which a regulated utility monopoly will have which are not as readily available to unregulated small business. In fact, they may not be available at all. The other witnesses this afternoon will provide examples of many of these marketing benefits which give the utility an unfair advantage.

IS THIS A NEW PROBLEM

In fact, the problem has been around for quite a number of years, but has become of increasing concern in the last few years. Like so many problems, they may subside, but they're soon back to haunt us unless we find permanent and long term solutions.

Let me give you an historical overview.

A major root of the problem is the competition between fuel types such as when the gas and the electric utilities each strive to maintain and increase their market share. For years, the competition between gas, electricity, and other fuel types has been intensive. Utility companies have relied on promotional practices, supply, installation, service, and financing programs to enhance their position in the market place.

At least once before in recent history, this has produced a public outcry resulting in congressional attention. In 1968, Congressman John Dingell conducted hearings on utility promotional practices before his Small Business Subcommittee, here in the House.

In the past, utilities promoted fuel consumption. More recently, the emphasis has shifted to energy conservation. Utility companies have attempted to move into the forefront in an attempt to promote energy conservation. To increase their market share, they strive to make their power source more economical and to lock consumers into their fuel type. This pressure to promote energy conservation while building market share has been increased further by well-intentioned public officials. Energy conservation programs were developed which gave inadequate attention to the effect on competition.

In 1978, Congress passed legislation creating the Residential Conservation Service which requires utilities to offer energy audits. Although the legislation had provisions prohibiting utility supply and installation, numerous loopholes make those prohibitions virtually meaningless.

Meanwhile, the legislation mandates that the rate payers subsidize energy audits provided by utilities which are in competition with those offered by small business. A utility cannot charge more than \$15 for an audit which costs a minimum of \$100 to \$150 to provide.

In 1980, Congress followed up on that by creating the Commercial and Apartment Conservation Service (CACS). This program even further enhances utility involvement by requiring audits of multi-family dwellings and small commercial establishments. Furthermore, in its haste to promote energy conservation, Congress made a major oversight regarding competition. Congress failed to include even the weak anticompetitive protections which were included in the RCS program.

By next month, states are supposed to submit state plans for implementing CACS. Despite a Department of Energy cautionary note and recommendations from the Small Business Administration Office of Advocacy, few have anticompetitive restrictions in them.

Utilities will be free to offer not only audits to our customers, but also to use the in-home and in-the-business audits as marketing opportunities to promote their own supply, installation, and service programs.

To combat unfair competition problems, the Alliance for Fair Competition was formed. The coalition has been aggressively attacking the problem on several fronts:

(1) Small businesses are forming coalitions in their local areas to meet with utilities and to intervene in state regulatory proceedings.

(2) When utilities wanted changes in the Public Utility Company Holding Act (PUHCA), the coalition met with utility representatives to fashion compromise language that would provide anticompetitive protections.

(3) Last summer, we met with Federal Trade Commission staff. As a result of the evidence we provided to the Commission, the FTC is now conducting an investigation of utility practices. They are expected to select several cases to pursue.

(4) The Senate Small Business Committee, chaired by Sen. Lowell Weicker, conducted hearings on utility competition last November.

(5) We provided comments to the SBA Office of Advocacy to assist them in producing their March report on "Utility Competition with Small Business".

(6) We have provided Congress with amendments for the RCS and CACS legislation which would prohibit use of utility programs to compete unfairly with small business.

(7) Today, this subcommittee is responding to the concerns that have been expressed by conducting this hearing to examine them.

ISN'T THIS A STATE ISSUE

Why isn't this a state issue rather than a federal issue?

It is, in fact, a state issue in many states as small businesses initiate and intervene in state commission proceedings. However, unfair utility competition is also an issue for federal public policy concern:

(1) when state commissions decline to consider the issue of competition or conclude that they do not have authority over the unregulated activities;

(2) when utility practices violate the antitrust laws;

(3) when Congress requires utility activity;

(4) when utility activities cross state lines preventing effective regulation by a state commission.

HOW IS THE CONSUMER AFFECTED

It is also a consumer issue. If utilities are permitted to control the market or limit competition, consumer choice is reduced. Yet the consumer has been required by the state regulatory commission to subsidize the indirect costs of the utility to conduct its unregulated activities which are now reducing consumer choice.

The consumer would be better served if the unregulated activities of a utility are expensed at full market based costs and credited to the utility function. If a bill stuffer goes with the utility bill, all of the costs for the bill stuffer, postage, and mailing would be charged to the unregulated activity. Such a proposal would lower rates since many of the indirect costs would no longer be charged to the rate payer, but to the unregulated activity.

RECOMMENDATIONS

(1) We fully support the March, 1984 report by the Chief Counsel for Advocacy of the Small Business Administration which recommends that utilities should be prohibited from sales, installation, or service. These, plus auditing, financing, and fuel switching efforts have resulted in unfair and anticompetitive programs that critically injure small business. Utilities should adhere to their primary mission of supplying energy and power to consumers.

(2) Antitrust enforcement should be pursued with deliberate speed before there is irreparable injury to competition.

(3) Congress should strengthen the antitrust laws to prohibit utility monopolies (protected from competition) from using their regulated companies to compete in unregulated markets. Antitrust laws should restrict the anticompetitive effects of marketing practices of big business monopolies.

(4) Congress should amend the RCS and CACS programs to build in the strong anticompetitive protections necessary or it should repeal the programs altogether to remove the federal implied approval of unfair utility practices which these programs provide.

Again, thank you for scheduling this hearing. Now members of the coalition will tell you how this problem affects them in their communities.

PURPOSES

To combat anticompetitive and unfair trade practices by utilities.

To develop a clearinghouse of examples and case studies which can be used by others involved in the effort.

To assist state and local associations and small businesses to ward off anticompetitive and unfair practices through public service/utility commissions, legislative bodies and litigation.

To work with the Congress and federal agencies to get action on unfair and anti-competitive practices.

MEMBERS

National Association of Plumbing-Heating-Cooling Contractors
 American Supply Association
 Air Conditioning Contractors of America
 American Consulting Engineers Council
 American Subcontractors Association
 Associated Specialty Contractors
 Door and Hardware Institute
 Independent Electrical Contractors Association
 Mechanical Contractors Association of America
 National Construction Industry Council
 National Lumber and Building Material Dealers Association
 National Oil Jobbers Council
 National Association of the Remodeling Industry
 National Electrical Contractors Association
 Northamerican Heating and Airconditioning Wholesalers
 Plumbing Manufacturers Institute
 Sheet Metal and Air Conditioning Contractors National Association
 Small Business Legislative Council

MEMBERS OF THE ASSOCIATED SPECIALTY CONTRACTORS

Mason Contractors of America
 Mechanical Contractors Association of America
 National Association of Plumbing-Heating-Cooling Contractors
 National Electrical Contractors Association
 National Insulation Contractors Association
 National Roofing Contractors Association
 Painting and Decorating Contractors of America
 Sheet Metal and Air Conditioning Contractors National Association

MEMBERS OF THE NATIONAL CONSTRUCTION INDUSTRY COUNCIL

American Concrete Pavement Association
 American Consulting Engineers Council
 American Rental Association
 American Road and Transportation Builders Association
 American Society of Civil Engineers
 American Subcontractors Association
 Associated Builders and Contractors
 Associated Equipment Distributors
 Associated General Contractors of America
 Associated Landscape Contractors of America
 Association of the Wall and Ceiling Industries, International
 Construction Industry Manufacturers Association
 Door and Hardware Institute
 Mechanical Contractors Association of America
 National Asphalt Pavement Association
 National Association of Minority Contractors
 National Association of Plumbing-Heating-Cooling Contractors
 National Association of Surety Bond Producers
 National Association of Women in Construction
 National Constructors Association
 National Electrical Contractors Association
 National Society of Professional Engineers
 Portland Cement Association
 Prestressed Concrete Institute
 Sheet Metal and Air Conditioning Contractors National Association

MEMBERS OF THE SMALL BUSINESS LEGISLATIVE COUNCIL PUBLICLY SUPPORTING FAIR
COMPETITION BY UTILITIES

American Association of MESBIC's
Architectural Precast Association
Automotive Service Councils, Inc.
Business Advertising Council
Christian Booksellers Association
Direct Selling Association
Eastern Manufacturers and Importers Exhibit
Electronic Representatives Association
Florists' Transworld Delivery Association
Independent Bakers Association
Independent Sewing Machine Dealers Association
Institute of Certified Business Counselors
International Association of Trade Exchanges
Ibero-American Chamber of Commerce
Latin American Manufacturers Association
Manufacturers Agents National Association
Menswear Retailers of America
National Association of Chemical Distributors
National Association of Plumbing-Heating-Cooling Contractors
National Association of the Remodeling Industry
National Council for Industrial Innovation
National Electrical Contractors Association
National Independent Dairy-Foods Association
National Office Products Association
National Oil Jobbers Council
National Small Business Association
National Society of Public Accountants
National Spa & Pool Institute
National Tooling and Machining Association
Power and Communications Contractors of America
Urethane Foam Contractors Association

Mr. LUKEN. Mr. Greene?

TESTIMONY OF BILL GREENE, VICE PRESIDENT, CENTRAL ROOF-
ING & SIDING CO., AND MEMBER, NATIONAL ASSOCIATION OF
THE REMODELING INDUSTRY, ACCOMPANIED BY JAMES TOL-
LIVER, EXECUTIVE DIRECTOR, NARI

Mr. GREENE. Thank you, Mr. Chairman and members of the sub-
committee.

Mr. LUKEN. You are with the Association of the Remodeling In-
dustry?

Mr. GREENE. That is correct; yes, sir.

I am Bill Greene, vice president of Central Roofing & Siding Co.
of Rockville, MD, and it is my privilege to appear today before
your Subcommittee on Antitrust and Restraint of Trade Activities
Affecting Small Business, representing the National Association of
the Remodeling Industry.

I also serve as chairman of the NARI legislative committee, and
I am accompanied here today by Mr. James Tolliver, NARI execu-
tive director, to my left.

NARI welcomes the opportunity to testify today at this hearing
on regulated monopolies competition with small business, and we
particularly appreciate the continuing interest of Chairman Luken
about the concerns of our association and industry on the impor-
tant issue of anticompetitive practices experienced by small busi-
nesses.

The National Association of the Remodeling Industry is a nationwide trade association representing all segments of the remodeling industry. NARI has approximately 4,000 contractor members as well as 75 members from the ranks of manufacturers, wholesalers, and distributors of building products.

It is, however, important to note that the heart of our association—our contractor members—are small businesses and enterprises in every sense of the word.

NARI has long been active in energy conservation activities, including previous testimony to congressional committees and the U.S. Department of Energy, and our membership continues to express our concern by NARI's active involvement with the Alliance for Fair Competition over the issue of utility competition with small business.

As a matter of fact, Mr. Chairman, we feel that NARI is largely responsible for bringing this matter to the attention of this subcommittee.

I speak from the heart when I get to this section here. Twenty-eight years ago, my father started a small remodeling business here in the metropolitan Washington, D.C. area.

Today we are facing a tremendous and—I hasten to add—a growing problem, not only for our company but for thousands of small, independent contractors throughout the country. Anticompetitive practices are being felt by other professional remodelers in many geographic areas of the country, and specifically in Massachusetts, Florida, Minnesota, New York, Wisconsin, and Oregon. However, I would like to concentrate my testimony on examples that I have personally experienced.

In the late 1970's, Washington Gas Light Co., one of the largest utilities serving the metropolitan Washington, DC area, decided to diversify into nonutility businesses—specifically, the sale and installation of insulating materials—through their purchase of Davenport Insulation Co.

Over time, this utility and their diversification programs have grown into one of the largest threats our industry has known.

Davenport Insulation, which has consistently been losing money since its takeover by the utility, is a prime example, in my opinion, of cross-subsidization.

Another subsidiary of Washington Gas Light Co. is Energy Conservation Systems. This is a separate company that they also formed. Both are in direct competition with me.

These two companies offer similar services and advertise under the same parent company. The advantages they have over me and other remodelers are numerous and unfair.

The utility advertises heavily in the major Washington newspapers, and I am sure the same advertising occurs in the media in other locations throughout the country. Obviously, this is something I cannot financially afford as a small businessman.

Here are specific examples of what I am talking about. Utility newspaper advertisements for energy conservation services such as windows, doors, siding, roofs, reroofing, and now even kitchen remodeling.

Included in my testimony are the attachments A through F, and they are in the back.

All these cited services are under the guise of energy conservation when, in fact, they are blatant examples of specific competition with the traditional role and function of the professional remodeler.

The utilities insert advertising under the same postage and handling in which their customers receive their monthly gas billing. I have before me an example of what I am talking about concerning subsidized advertising inserts.

Mr. LUKEN. May I ask, what is the entity or the corporate status of the Washington Gas business? Is this a subsidiary?

Mr. GREENE. Yes. Washington Gas Light being the utility, they have two subsidiaries—one, Davenport Insulation Co., the other is Energy Conservation Systems; that's another subsidiary.

Mr. LUKEN. There are two subsidiaries that do the same thing.

Mr. GREENE. That is correct. Yes, sir.

Not only do I feel that they are in competition with me, but I think that at times they are in competition with each other.

Mr. LUKEN. They advertise Washington Gas.

Mr. GREENE. That is correct.

If you will notice—

Mr. LUKEN. They don't use the subsidiary corporate name in the advertising; they use the logo of the monopoly?

Mr. GREENE. Yes, sir. They use the logo as the large portion of their ad. However—you do have the ads in front of you there, sir—you will notice that in smaller type their subsidiary is listed, but it is the parent company that they are stressing in their ads.

Mr. LUKEN. They do, in effect, what we always prohibited Ma Bell from doing. Ma Bell was never permitted to get into any auxiliary services.

Mr. GREENE. No.

Mr. LUKEN. They are only in it since they have been required to divest?

Mr. GREENE. Yes, sir.

Mr. LUKEN. In other words, divest their regulated from their unregulated.

Mr. GREENE. I do have attached copies of their advertising at the end of my testimony.

Mr. LUKEN. Thank you for allowing me to interrupt.

Mr. GREENE. Sure.

The ones that are, you know, disturbing to me is the insert that I recently received in my gas bill, and this is a prime example of a utility using a readymade mailing list of thousands of potential customers, and I could never accumulate such an extensive list; nor could other remodelers.

Let me hypothesize about a marketing director's dream situation. The marketing abilities utilities have with their computerized database and through the Residential Conservation Service—the RCS Program—and now the Commercial and Apartment Conservation Service Program, afford utilities the opportunity to identify potential customers far beyond the capabilities of the small businessman, such as myself.

I do not believe it was the intent of Congress when they enacted the RCS and CACS programs to afford the utilities carte blanche

means to offer to sell consumers the same energy-saving materials they recommend in their home energy audits.

Obviously, it is very attractive for utilities to offer their audit recommendations through their installation departments, bypassing the State-required list of approved contractors.

The audits also give the utility the inside demographic information they need to target their marketing area.

Another example of anticompetitive practices I face is that the utility provides their management and sales staff a fleet of company vehicles and utilize utility personnel for dual duties. I cannot be convinced that there is not an overlapping of management and technical personnel, equipment, and resources.

Yet another example is their telephone directory advertising. You will find that the ads are listed under the utility and not under the diversified companies, which you mentioned earlier. It is under the utility itself and not under the diversified companies.

This is confusing and misleading to the average consumer, because they feel they are dealing with the utility and not a subsidiary of the company itself.

A final example is the utility's ability to offer the customer financing at no interest for a short term and for rates below those commercially available for longer term loans. These payments can be made very conveniently as part of the monthly utility bill.

I hope these examples of anticompetitive practices will be proof enough that there is a problem.

As a small businessman, I assure you, I strongly believe in the spirit of American free enterprise. I speak not only for myself and for the members of NARI but for the thousands of fellow contractors and small businesses throughout this country.

We are forced to attempt to compete in an atmosphere which is totally unfair with the utilities while they enjoy their numerous advantages because of cross-subsidization operations, some of which I have cited in my testimony. It seems we are fighting a growing battle against monopolistic giants and not against our fellow competitors.

Just 28 years ago, my dad started Central Roofing & Siding Co. and passed our family business on to me, and I likewise hope some day to pass our business on to my son.

On behalf of fellow NARI members as well as small businesses everywhere in the Nation, I respectfully request that this subcommittee and the Congress as a whole consider the effects that monopolies competition are having on small businesses.

Thank you very much for allowing me, representing NARI, the opportunity to appear before this distinguished Subcommittee on Antitrust and Restraint of Trade Activities Affecting Small Businesses today to discuss the plight remodelers are facing every day to make ends meet in the face of unfair competition in the marketplace.

Mr. Luken, if you have any questions.

Mr. LUKEN. Well, we will question you further when we are finished. I was just interjecting an informal, unscheduled one there.

Mr. GREENE. OK.

[Mr. Greene's prepared statement with attachments follows:]

PREPARED STATEMENT OF BILL GREENE, VICE PRESIDENT, CENTRAL ROOFING & SIDING CO., AND MEMBER, NATIONAL ASSOCIATION OF THE REMODELING INDUSTRY

Mr. Chairman and members of the Subcommittee, I am Bill Greene, Vice President of Central Roofing and Siding Company of Rockville, Maryland. It is my privilege to appear today before your Subcommittee on Antitrust & Restraint of Trade Activities Affecting Small Business representing the National Association of the Remodeling Industry (NARI). I also serve as chairman of the NARI Legislative Committee. I am accompanied today by Mr. James Tolliver, NARI Executive Director.

NARI welcomes the opportunity to testify today at this hearing, "Regulated Monopolies Competition with Small Business," and we particularly appreciate the continuing interest of Chairman Luken about the concerns of our association and industry on the important issue of anti-competitive practices experienced by small businesses.

The National Association of the Remodeling Industry (NARI) is the nation-wide trade association representing all segments of the remodeling industry. NARI has approximately 4,000 contractor members, as well as 75 members from the ranks of manufacturers, wholesalers and distributors of building products. It is, however, important to know that the "heart" of our association—our contractor member—are small businesses and enterprises in every sense of the word.

NARI has long been active in energy conservation activities, including previous testimony to congressional committees and the U.S. Department of Energy, and our membership continues to express our concern by NARI's active involvement with the Alliance for Fair Competition over the issue of utility competition with small business. As a matter of fact, Mr. Chairman, we feel that NARI is largely responsible for bringing this matter to the attention of this Subcommittee.

Twenty-eight (28) years ago my father started a small remodeling business here in metropolitan Washington, D.C. Today we are facing a tremendous, and I hasten to add, a growing problem—not only for my company—but for thousands of small independent contractors throughout the country. Anti-competitive practices are being felt by other professional remodelers in many geographic areas of the country, and specifically in Massachusetts, Florida, New York, Wisconsin and Oregon. However, I would like to concentrate my testimony here today before your Subcommittee on examples I have personally experienced.

In the late 1970's Washington Gas Light Company, one of the largest utilities serving the metropolitan Washington, D.C. area, decided to diversify into non-utility businesses. Specifically, the sale and installation of insulating materials through their purchase of Davenport Insulation. Over time, this utility and their diversification programs have grown into one of the largest threats our industry has known.

Davenport Insulation which has consistently been losing money since its takeover by the utility, is a prime example, in my opinion, of cross-subsidization. Another subsidiary of Washington Gas Light Company is Energy Conservation Systems. Both are in direct competition with me. These two companies offer similar services and advertise under the same parent company. The advantages they have over me, and other remodelers, are numerous and unfair.

The utility advertises heavily in the major Washington newspapers. I am sure the same advertising occurs in the media in other locations throughout the country. Obviously, this is something I can not financially afford as a small businessman.

Here are specific examples of what I am talking about; utility newspaper advertisements for energy conservation services such as windows, doors, siding, roofs and re-roofing, and now even remodeling of kitchens. I have attached advertisement examples as "Attachments A-F" to the testimony.

All these cited services are under the guise of energy conservation when, in fact, they are blatant examples of specific competition with the traditional role and function of the professional remodeler.

They (utilities) insert advertising, under the same postage and handling, in which their customers receive their monthly gas billing. I have before me an example of what I am talking about concerning subsidized advertising inserts. I have attached this example as "Attachment G" to my testimony. This is an insert for kitchen remodeling which I recently received in my gas bill. This is an example of a utility using a ready-made mailing list of thousands of potential customers. I can never hope to accumulate such an extensive list nor could other remodelers.

Let me hypothesize about a marketing director's dream situation. The marketing abilities utilities have with their computerized data base, and through the Residential Conservation Service (RCS) and the Commercial and Apartment Conservation Service (CACS) programs affords utilities the opportunity to identify potential customers far beyond the capabilities of the small businessman, such as myself.

I do not believe it was the intent of Congress when they enacted the RCS and CACS programs to afford the utilities "carte blanche" means to offer to sell consumers the same energy-saving materials they recommend in their home energy audits. Obviously, it is very attractive for utilities to offer their audit recommendations, through their installation subsidiaries, by-passing the state-required list of approved contractors. The audits also give the utility the "inside" demographic information they need to target their marketing area.

Another example of anti-competitive practices I face is that the utility provides their management and sales staff a fleet of company vehicles, and utilize utility personnel for dual duties. I can not be convinced that there is not an overlapping of management and technical personnel, equipment and resources.

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We are forced to attempt to compete in an atmosphere which is totally unfair with the utilities while they enjoy their numerous advantages because of cross-subsidization operations, some of which I have cited in my testimony. It seems we are fighting a growing battle against monopolistic giants, and not against our fellow competitors.

Just as 28 years ago my father started Central Roofing and Siding Company and passed our family business on to me—his son—I, likewise, hope that one day I can also pass our family company on to yet another generation of the Greene family—my son.

On behalf of my fellow NARI members, as well as small businesses everywhere in the Nation, I respectfully request that this Subcommittee, and the Congress as a whole, consider the effects that monopolies competition are having on small businesses.

Thank you very much for allowing me, representing NARI, the opportunity to appear before this distinguished Subcommittee on Antitrust & Restraint of Trade Activities Affecting Small Business today to discuss the plight remodelers are facing every day to make ends meet in the face of unfair competition in the market place.

A16

Monday, October 19, 1981

THE WASHINGTON POST

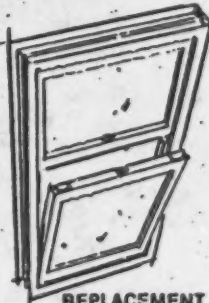
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Let us tell you how to help cut those heating and cooling bills, regardless of the fuel you use. You'll be eligible for a Federal Income Tax credit of up to \$300.

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We sell, install and finance total insulation systems: Home Insulation, Windows and Doors, Aluminum and Vinyl Siding with Insulation.

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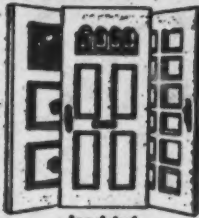
WHILE SUPPLY LASTS 1100 H STREET, N.W., WASHINGTON, D.C. 20080

DOORS, DOORS & MORE DOORS

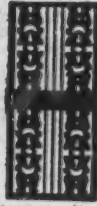
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Save fuel dollars.**

Attachment C

Wrap your home in insulation with the new Thermal Wall System!

Here's how a Thermal Wall System insulates your home. The Thermal Wall insulation panels are applied over your home's existing exterior walls. Then a new exterior covering is applied with your choice of VYNAL-KLAD Aluminum or Premium Vinyl material over the Thermal Wall panels. This gives your home a beautiful new exterior finish. Gaps between windows and doors are effectively sealed to help reduce air leakage. The result is the ultimate in energy conservation and thermal protection for the exterior of your home. Enhance your home with a Thermal Wall System today and realize energy savings year after year.



NO DOWN PAYMENT. CONVENIENT LONG-TERM PAYMENT PLAN

MAIL THE ATTACHED CARD TODAY.

A gas company Sales Representative will call you for an appointment. You will be given the cost in advance. You can pay cash (in three equal monthly installments) or use our convenient long-term payment plan.

Washington Gas

LINEC 8830

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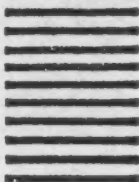
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Attachment
D

Washington Gas sells, installs and finances home insulation, storm windows and doors and replacement windows.

Insulate walls, attic and crawl spaces.



Most homes in the Washington area were built before the sharp increase in energy costs. In most cases, these homes are inadequately insulated by today's standards.

Re-insulation of your home can help you hold down your heating and cooling bills—regardless of whether you use gas, electricity or oil.

Just complete and return the attached card and a gas company Sales Representative will contact you to make an appointment. He'll give you a specific recommendation if your home needs additional insulation and tell you how much it will cost.

Exterior doors need storm doors.

Storm doors help prevent heat loss by reducing infiltration of cold winter winds. And in the autumn and spring, storm doors with interchangeable glass/screen panels let you enjoy the fresh air on pleasant days.

Replace those drafty old windows.

A major source of heat loss and cold air infiltration can be old windows that have lost their effectiveness. Now is the time to replace them with thermally improved windows.

In terms of cost, it may be considerably cheaper to replace your old windows than to scrape, paint and caulk your old windows and add storm windows. In addition, replacement windows are virtually maintenance-free—never need repainting.

...or add storm windows.

If your present windows are in good condition, the addition of storm windows may be all that you need to cut down heat loss and air infiltration.



NOTE: Buy now and take advantage of the Federal Tax Credit for energy conservation products. The credit amounts to 15% of the first \$2,000 of expenditures with a maximum of \$300.00.



I am interested in cutting my heating and cooling bills. Please have a Sales Representative call me for an appointment.

- ☐ Insulating my attic.
- ☐ Thermal Wall System.
- ☐ Insulating crawl spaces.
- ☐ Replacing windows.

Name _____

Address _____

City _____

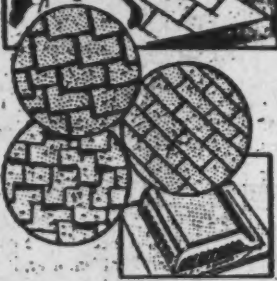
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Buy Now! Pay Later!

No payments until January 1984.

**Let Washington Gas
beautify and protect
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with new
roofing
shingles.**



- Wide choice of attractive, tough asphalt and fiberglass shingles.
- Different styles, colors and textures available.
- New ventilation system included: reduces energy consumption in summer and prevents annoying condensation build-up in winter.

WE SELL, INSTALL AND FINANCE:

Insulation, Thermal Siding, Thermal Roof Systems,
Storm Windows & Doors and Thermal Replacement Windows & Doors.

NO DOWN PAYMENT.

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TO QUALIFIED CREDIT APPLICANTS.**

Call 354-5700 Today!

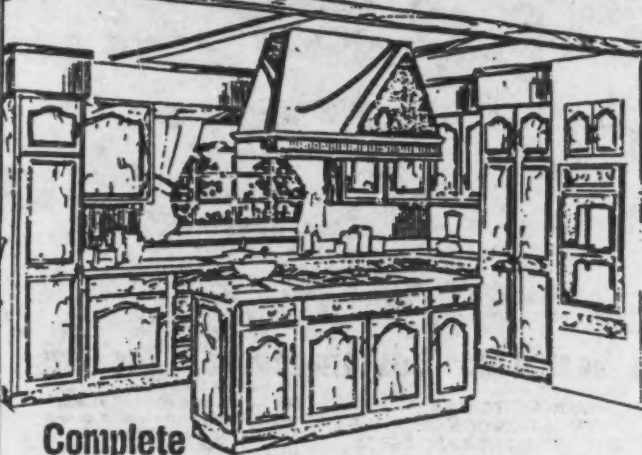
OUTSIDE METRO AREA CALL (703) 354-5700



Washington Gas
ENERGY CONSERVATION SYSTEMS

SMC L.C. 99990

Let Washington Gas remodel your kitchen.



Complete kitchens with installation of modern energy-efficient appliances.

We'll create a custom-designed kitchen for you!

Here's what we'll arrange:

- ☐ Free estimate and design service.
- ☐ Kitchen remodeling, just the way you want it.
- ☐ Installation of energy-efficient appliances.
- ☐ Variety of cabinets in your choice of finish and color.

NO DOWN PAYMENT.

CONVENIENT LONG-TERM PAYMENT PLAN TO QUALIFIED CREDIT APPLICANTS.

WE SELL, INSTALL AND FINANCE:

Insulation, Thermal Siding, Thermal Roof Systems, Storm Windows & Doors and Thermal Replacement Windows & Doors.

Call 354-5700 Today!

OUTSIDE METRO AREA CALL (703) 354-5700

FORECAST KITCHENS FROM



Washington Gas
ENERGY CONSERVATION SYSTEMS

MHC Lic #9850

Attachment 6



**Washington
Gas**

P.O. Box 2422
Washington, D.C. 20001

POSTAGE
PAID PERMIT
NO. 1000
WASHINGTON, D.C.



Let Washington Gas remodel your kitchen.

COMPLETE KITCHENS WITH INSTALLATION OF MODERN ENERGY-EFFICIENT APPLIANCES.

- Fine cabinets in your choice of finishes and colors.
- Counter tops in your choice of colors and materials.
- Free estimate and design service.

NO MONEY DOWN.

Convenient long-term payment plan to
qualified credit applicants.

FORECAST KITCHENS FROM



Washington Gas
ENERGY CONSERVATION SYSTEMS

SMC LG 10000

003200

To have a sales representative contact
you, please fill out the form below and
mail this postage-paid reply card.
No obligation.

Name

Address

City

State Zip Code

Home Phone

Work Phone

Mr. LUKEN. Mr. Jim Johnson, you are from Seymour, IN?

Mr. JOHNSON. That is correct.

Mr. LUKEN. It's almost in the tri-State area, isn't it?

Mr. JOHNSON. Yes, sir.

Mr. LUKEN. Welcome to Washington.

TESTIMONY OF JAMES A. JOHNSON, PRESIDENT, MIDWAY SUPPLY CORP., AND MEMBER, AMERICAN SUPPLY ASSOCIATION, ACCOMPANIED BY PATRICK C. O'CONNOR

Mr. JOHNSON. Thank you. I appreciate the invitation to be here today, and I have quite a lengthy statement up there, and I am not going to go through all that.

Mr. LUKEN. Well, it will be received into the record. So if you will, just summarize it.

Mr. JOHNSON. I shall do that.

I am Jim Johnson. I am president of Midway Supply Corp. We are pleased to be celebrating our 30th year in 1984. We serve as a wholesale distributor for southern Indiana, and we are selling to retail merchants, dealers, and installing contractors.

Our product line includes plumbing, heating, air conditioning, piping, appliances, and kitchen cabinets. We are what you would consider a traditional type supply house in size and the fact that we have 17 employees, and also in our product mix you would consider us traditional.

In our 30 years, we have yet to lay off our first employee, and we have 130 years of combined service in those people to our company.

We are also a member of American Supply Association, which has 1,200 members nationwide.

It's like a blitzkrieg throughout our country. Gas and electric utility companies are venturing from the production and distribution of energy into the sale of appliances. Wholesalers throughout the country are facing this direct competition.

I have enclosed a list at the end of my statement that indicates some of the areas where there is concern. It also shows a map to show the intensity in some of those areas.

At Midway we have special concern. Our customers share this concern. The Indiana Gas Co. has entered into the retail sales of products that are currently sold through existing channels.

Indiana Gas Merchandise Program includes hot water heaters, gas grills, dishwashers, ranges, washers, dryers. I have included an announcement of this venture as one of my appendices. It appeared on November 8 in our local newspaper.

There are some interesting things that can be drawn from these advertisements. Indiana Gas is not only selling gas appliances, it is selling dishwashers which require no gas hookup. The total amount of the purchase can be put on the Indiana Gas monthly bill. This of course—

Mr. LUKEN. Directly or through a subsidiary?

Mr. JOHNSON. Directly. You are dealing with the Indiana Gas Co.

Mr. LUKEN. You are sure of that?

Mr. JOHNSON. Yes, sir.

Mr. LUKEN. I'm not doubting you, but just to make sure you have taken pains to make sure what the corporate status is.

Mr. JOHNSON. Yes, I have.

They have talked about the advantages of this being on the monthly bill. There are some very distinct ones. You don't have to have a credit card in your hand, there is no waiting period, there is no credit application, and the interest rate is very attractive.

On the appendices, it shows that their advertisements say that there is 30 days no interest. In comparison shopping, we find it is actually 90 days no interest. Additionally, a full year at 9.9-percent interest and a 3-year monthly payment, if you work it out, comes out to less than 10 percent interest. That is considerably below the consumer loan rate in our area.

Bank loans for consumer items are 16 to 18 percent; finance companies, 21 to 24 percent; bank credit cards, 19 to 21 percent; and 9.9 is not only below all those rates, but it is about 20 or 25 percent below the current prime rate in our area.

Another observation is the advertising of the gas company has changed. Prior to November 8, they were doing information type advertising on Tuesdays. Now on Tuesdays, we have advertising that is promoting the sale of dishwashers, water heaters, et cetera.

It appears that they purchased a Tuesday block and then diverted this advertising to the retail segment.

There are some additional concerns that our installing contractor has in the fact that he receives simply an installation fee. He is denied the markup on the unit.

The gas company has a prequalifying system to place a contractor on their installation list. Then the gas company selects whom ever they choose to install the sale. This removes the potential customer from the marketplace for the dealer, retail store, contractor, and ourselves. Moreover, it's all done at an interest rate that is below the going amount.

The gas company indicates that they are doing their service with in-house people. This appears to be a subsidized type of service department.

I use Seymour's as an example, but we can find similar examples throughout the area that Indiana Gas services. I understand that you have a picture up there that shows the front of the Muncie store. If you will notice in that closeup, it talks about a gas grill sale.

We feel that our industry is very efficient, cost effective, and a service-oriented network. We also know how slim our profit margins are.

In 1982, the average sale of an ASA member was around \$4 million. Their profits were 1 percent of sales. Competition of the nature that a utility brings to our marketplace is devastating. My concern is that the Indiana Gas Co. has far more financial resources than we or our dealers; plus, they have a lock on their customers. They can easily use retail product sales as a loss and then roll it, in effect, in their rate base.

The Indiana Public Service Commission has a pretty cut-and-dried approach to it. No prior approval is required to engage in merchandising or jobbing, and because it is a nonutility operation, the public service commission has no authority over how this business is run or its impact on the small-business competitors. There is one requirement. That is, its activities are shown below the line.

They can use personnel, equipment, share overhead, and lack of clear-cut written guidelines, and because the Indiana Public Service Commission considers the dollar amount involved too inconsequential to merit strict scrutiny, there are many hidden costs of the appliance business which can be absorbed by the utility.

According to the Indiana Public Service Commission, the utility appliance businesses are not profitmaking endeavors, with most barely making it past the break-even point. Their intent in having the business is to promote the use of gas, not to build a successful appliance merchandising business. Therefore, the utility can sell the product at below cost, provide market financing, and generally offer enticing deals which no competing small business can possibly match.

A review of the Indiana law reveals that there is no clear-cut statutory authority for the Indiana Public Service Commission to examine the effect of nonutility operations on small business competitors.

Mr. Luken and Mr. Weber, the maintenance of a competitive market is a valid public policy concern. Unless a utility's entry into my business and into the business of other small businesses is subjected to the terms and conditions to preclude cross-subsidization and anticompetitive practices, then the utilities should not be allowed to cross the line from regulated to unregulated business.

The proposals offered today by Chief Counsel Frank Swain are positive approaches, but they require commitment from Congress and Federal agencies and the States to see that these proposals move beyond this hearing room.

Thank you again for having me.

[Mr. Johnson's prepared statement with attachments follows:]

PREPARED STATEMENT OF JAMES A. JOHNSON, PRESIDENT, MIDWAY SUPPLY CORP., AND
MEMBER, AMERICAN SUPPLY ASSOCIATION

Mr. Chairman, thank you for your invitation to appear here today. I am Jim Johnson, President of Midway Supply Corporation. Midway Supply is celebrating it's 30th year in 1984 and serves southern Indiana as a wholesale distributor to retail merchants, dealers, and installing contractors.

Our product line includes plumbing, heating, air conditioning, piping, appliances, and kitchen cabinets. We are a traditional type supply house in size, as well as product mix, with 17 employees and annual sales of \$2,700,000.00. Our employees have a combined service of 130 years with the company and Midway has yet to lay off an employee, even though we are in a very cyclical business. We are also very proud of our standing in our community of Seymour, where we are located.

Midway Supply Corporation is a member of the American Supply Association. ASA is the single, national association representing suppliers and distributors of plumbing, heating and cooling products to contractors, industrial, educational and institutional users. There are 1200 members of the Association with four thousand locations in all fifty states. ASA member companies are almost all small, family-owned businesses. In 1982, the typical company had sales of \$4 million and showed a net profit—after taxes—of 1%.

My company is also a member of the Central Wholesalers Association, which represents the States of Ohio, Indiana, Kentucky, West Virginia, as well as parts of Illinois and Pennsylvania.

Like a blitzkrieg throughout the country, gas and electric utility companies are venturing from the production and distribution of energy into the sale, installation and service of gas and electric appliances, products and systems. Wholesalers and suppliers throughout the country are seeing their profits decrease and their businesses threatened as utilities have become our direct competitors. As an attachment to my testimony, I have enclosed a list of utilities identified by ASA members as being in direct competition. This last item is supplemented with a map which

graphically displays the extent of utility merchandising programs across the country.

Today, we at Midway Supply, as well as our customers, are greatly concerned. This concern stems from the fact that Indiana Gas Company has entered the retail sales of products that are currently sold through existing channels. Indiana Gas' merchandising program includes hot water heaters, gas grills, dishwashers, ranges, washers, and dryers. I have included an announcement of this venture (as Appendix "B"), that appeared in the Seymour Daily Tribune on Tuesday, November 8, 1983, as well as additional advertisements which have appeared in the Seymour Daily Tribune.

There are several interesting observations that can be made from these advertisements:

1. Indiana Gas is selling some items which cannot be connected to a gas service. Note in Appendix "C" that they mention dishwashers which require no gas.

2. The total amount of the purchase can be added to the customers monthly gas bill. Appendix B, C, D, E, G, H. There is a great advantage to the ease in which they can do this with no credit application, no waiting period, or no credit card possession.

3. The gas company offers 30 days no interest on purchases (See Appendix "C"). In comparison shopping, we found that the gas company was actually allowing 90 days no interest and Appendix "I" shows this in the handwriting of the sales person whose card is shown in Appendix "J".

4. The interest rate on the installment purchase is considerably below the going rate in our area. Appendix "I" shows not only 90 days at no interest, but shows additionally a full year at 9.9%. The monthly payment shown at the right of Appendix "I" indicates an interest rate below 10% for all three years on not only the unit, but the installation cost, as well. Comparable interest rates on consumer loans in our area since mid-November run as follows:

Bank Consumer Loans: 16-18%.

Finance Companies: 21-24%.

Bank Credit Cards: 19-21%.

The 9.9 percent runs not only far below the going consumer rate but also 20 percent or more below the prime rate in our area.

5. The advertising of the gas company changed. They previously were doing informational type of advertising every Tuesday, which is generally permitted to be charged to the ratepayer (See ad in Appendix "A"). After Tuesday, November 8, 1983, this Tuesday space was used to promote sales of appliances, dishwashers, water heaters, etc.

Appendix D, Tuesday, November 15, 1983

Appendix E, Tuesday, December 20, 1983

Appendix F, Tuesday, January 10, 1983

Appendix G, Tuesday, February 7, 1983

Appendix H, Tuesday, February 14, 1983

It appears they purchased a block of ads to run on Tuesday and diverted the space to the retail sales of appliances, water heaters, etc.

Additional concerns are that the installing contractor receives an installation fee only and is denied the mark up on the unit. The gas company has a pre-qualifying system to place a contractor on their installation list. Then the gas company selects whomever they choose to install the sale. This removes the potential customer from the market place of the contractor, dealer, and the retail store. Moreover, it is all done at below the going interest rate.

The gas company indicates they are using in-house service people, who regularly perform other tasks for the utility, to service the products the utility is retailing. This seems to be a subsidized service department.

We use Seymour as an example, but similar examples could be found for nearly all communities serviced by Indiana Gas. We feel our industry is a very efficient, cost effective, and service oriented network. We also know how slim our profit margins are. Competition of the nature that a utility brings to our market place is devastating.

My concern is that the Indiana Gas Company has far more financial resources than we and our dealers have. Plus, the gas company has a "lock" on all those who purchase gas from them when they are in the market for a new appliance. I also feel the gas company can easily use the entire retail product sales area as a way to sell gas and then roll those losses into their accounting to affect their rate base.

To the Indiana Public Service Commission, their treatment of a utility's appliance merchandising business is fairly cut and dry. No prior approval is required to engage in merchandising and jobbing. And because it is a non-utility operation, the

PSC has no authority over how that business is run, or its effect upon small business competitors. The only requirement is that all costs associated with the appliance business must be kept separate from the utility operation. In other words, the expenses and revenues are "below the line" for ratemaking purposes.

The utility can utilize its personnel, equipment and related overhead costs for its sales program, as long as the utility allocates the costs. However, there are very few written guidelines or policies to govern specifically how costs are to be allocated. And, over the years, these cost allocations have rarely been challenged. Advertising costs are the one area which have, on occasion, been disallowed. This has occurred when the utility charged to the ratepayer the costs (in one case amounting to nearly \$150,000) of advertisement promoting the products of the utility's appliance business.

Because of the lack of clearcut written guidelines and because the Indiana PSC considers the dollars amount involved too inconsequential to merit strict scrutiny, there are many hidden costs of the appliance business which will be absorbed by the utility. For example, the cost of a flyer inserted in the monthly gas bill is not likely to be borne by the appliance business. Nor will they have to pay for the expense of delivering an appliance when the utility's trucks are used. These kinds of costs are not easily allocated and with limited resources available, the PSC does not devote the necessary attention to seek out such costs and make certain they are kept separate.

According to the Indiana PSC, the utility appliance businesses are not profit-making endeavors, with most barely making it past the break-even point. Their intent in having the business is to promote the use of gas, not to build a successful appliance merchandising business. Therefore, the utility can sell the appliance at below cost, provide below market financing and generally offer enticing deals which no competing small business can possibly match.

A review of the Indiana law reveals there is no clear statutory authority for the Indiana Public Service Commission to examine the effect of non-utility operations on small business competitors. However, in a recent order of PSC, where utilities were permitted to begin a below market financing program (subsidized by ratepayers) for weatherization measures, the PSC did look at the competitive impact on other utilities. In deciding to exclude furnace replacement and active solar measures from the program, the Commission noted the "high level of competition concerning heating equipment and choice of heating systems" giving as examples NIPSCO's marketing of gas pulse combustion furnaces and IPL's heat pump market drive. Because of this, such measures were excluded from the weatherization loan program and the Commission reasoned:

"It is at least conceivable that a customer might receive a Weatherization Program loan from a utility only to install a new heating plant designed to use the service of another competing utility. In other words, the utilities might be cutting their own throats. Even limiting furnace replacement to the same type of service as the utility providing the loan might constitute an unfair market advantage." Public Service Commission of Indiana, Cause No. 37321, January 13, 1984, p. 6.

My problem and that of my fellow members of the ASA is that we cannot compete with the unfettered ability of a utility to use its rate paying customers to subsidize, whether directly or indirectly, the marketing and advertising campaigns directed toward particular consumers and products. I am not here to advocate protectionism or a reduction in competition. I welcome competition. Our industry thrives on competition as do all small businesses. My company and all of the companies in ASA have been built through initiative, hard work, the entrepreneurial spirit and fair competition. However, competition is only beneficial when all the participants have to play by the same rules. When a utility sells and installs appliances, its massive economic advantage subsidized directly or indirectly advantage beyond my reach. I don't believe it is in anyone's best interest to allow a regulated business to encroach undeterred on the unregulated sector. A utility company should not be allowed to take the first penny of ratepayer money and divert it to compete with unregulated small businesses.

The utilities' movement into business is motivated by the fact that their job is to sell energy. Their competitor in the local market is the other utility—e.g., gas versus electric. They are engaged in a constant battle to maintain customers, to increase energy sales and to convert customers from their competitor's energy source.

Indicative of the fierce competition between the various energy sources is the amount of money that goes into promotion. I am sure that the witnesses here today from EEI and AGA would attest to the fact that their respective yearly advertising budgets are for selling the benefits of gas and electricity.

The American Gas Association, in written testimony to the Senate Small Business Committee in follow-up to that Committee's November 1983 hearings on utility competition, stated that their members are involved in merchandising gas appliances and equipment to "preserve and protect gas markets". The fact of the matter is that the only means for a utility to preserve and expand its market for gas or electricity is to have the equipment at the end of the gas line or the electric cable. For example, a major source of energy consumption is a hot water heater. Every residence and every commercial and industrial establishment has a hot water heater of some type on site. A building owner has the choice of heating with either gas or electricity. It is this competition for the customer's business which leads utilities into the appliance business.

At this point, I would like to say that there are indeed utilities which promote the benefits of their energy source but rely solely on the private sector to market the appliances. Cooperative advertising programs, product displays, referrals, etc., have developed constructive relationships between utilities and private suppliers and contractors. Our problems arise when a utility company decides that suppliers and contractors aren't doing the job and then steps in to exert control over the appliance market. Using low cost financing, rentals, free installation and low cost maintenance programs, utilities have an anticompetitive impact on free enterprise.

When utility companies venture into traditional wholesale, retail and contracting functions they must be closely scrutinized because:

(1) Such programs are often and easily subsidized by passing through part of the costs to all ratepayers. A utility's rates will often absorb many of the research, development, administrative, marketing and product costs.

(2) When competing head to head with small businesses for the same customer, utilities—because of their protected monopoly status—enjoy a massive marketing advantage through their penetration into every home, office building and factory.

(3) Utility involvement in sales, installation and service of gas and electric products and systems to their customer base ensures a continued demand for their primary product to those same customers—energy.

Appliance operations of a utility are, however, rarely subject to the kind of scrutiny necessary to prevent anticompetitive effects on small business competitors or ratepayer subsidization of the appliance program. Traditional regulation of utilities does not adequately review pricing practices, marketing practices and ratepayer subsidies.

As in Indiana, the primary role of the public utility commission (PUCs) in other states has been to ensure that the ratepayers are not subsidizing the utility's unregulated business activities. The prevention of cross-subsidization is not uniform among the states. State public service commissions often lack the staff and resources necessary to prevent cross-subsidization. Further, there is no uniform agreement as to what cross-subsidization is or what it entails.

Cross-subsidization is difficult to define except in the most blatant cases. The difficulty in defining the term naturally leads to problems in regulating to prevent cross-subsidization. For any utility or public service commission to blithely say that appliance sales are "below-the-line", and not included in determining rates, ignores what a cross-subsidization is.

Cross-subsidization occurs when the utility provides financial, overhead or administrative assistance to the unregulated activity without the full market-based charge being imposed. This can include the underwriting of the costs and maintenance of equipment, personnel and office space. Such assistance can also take the form of the utility providing or obtaining noncompetitive financing for the unregulated activity, or the sharing of legal and accounting services.

Cross-subsidization can occur in the access to customer lists or credit information by the unregulated activity, or the use of the utility's billing, advertising or marketing resources without reimbursing the ratepayer at a market-based price. A cross-subsidy occurs when the unregulated activity conducts business using the name and identification of the utility, without reimbursement to the ratepayer.

In most states, anticompetitive and unfair practices are rarely addressed by public service commissions. While some PUCs either have the specific authority or have interpreted their authority as allowing them to look at competition, most PUCs have refused to consider claims based on competitive harm. Utility marketing and pricing practices are considered to be outside a state regulatory's authority. As the Federal Trade Commission stated in the Bureau of Competition Working Paper "Competition and Utility Cross-Subsidization of Energy Conservation Practices":

"There are at least two reasons for this position. First, there is no specific mention of competition in unregulated markets in PUC authorizing statutes; from this absence and the monopoly statutes of utilities, PUC officials may have drawn the

conclusion that they are unable to consider competition policy. Second, until recent years, regulated businesses were generally thought to be exempt from antitrust laws, under the state action doctrine enumerated in *Parker v. Brown* Although as discussed in *Canton V. Detroit Edison* and subsequent cases, the Supreme Court has significantly modified the doctrine, the states have not fully adjusted to this change."

In a recent proceeding before the New York State Public Service Commission (PSC), suppliers and contractors attempted to raise competitive arguments in opposition to a petition filed by Long Island Lighting Company to create LILCO Energy Systems. The decision by the New York PSC was:

"To assist the parties in preparing their evidentiary submission, we wish to emphasize that testimony which solely concerns the effects of competitors of the entry into the market of LILCO Energy Systems, Inc., is not of interest to the Commission in this proceeding." (State of New York Public Service Commission, order granting Requests for Evidentiary Hearings, issued January 13, 1982.)

Even upon vigorous appeal of this determination by the New York Attorney General, the New York Public Service Commission refused to consider the impact on small business competitors.

Where effective state regulation is lacking, the federal regulator must be prepared to fill the void. To date, however, existing federal antitrust authority has not provided an effective deterrent or remedy to anticompetitive practices by utilities. Uncertainty of the applicability of federal antitrust statutes to utilities regulated by State agencies has limited the effectiveness of federal antitrust laws. Also, the costs of private antitrust action virtually eliminates such actions as a realistic option for a small business. Litigation is expensive and time-consuming. A case in point: In Oklahoma, electrical contractors have battled in courts for over seven years and still their case, brought under Section 2 of the Sherman Act and Sections 4 and 16 of the Clayton Act, has not been settled. For a supplier to take the utility company to court, his legal costs have to come out of his bottom line while the legal fees incurred by the utility can be passed on to all ratepayers.

We believe that the Federal Trade Commission, using Section 5 of the Federal Trade Act, has the authority to look at utility trade practices which may be unfair or anticompetitive. As you have heard today, the FTC has begun a preliminary investigation into utility competition with small businesses. We hope that this subcommittee will keep in close contact with the Bureau of Competition during the course of this investigation.

Mr. Luken, the maintenance of competitive markets is a valid public policy concern. Unless a utility's entry into my business or into any other small business is subject to terms and conditions to preclude cross-subsidization and anti-competitive practices, then the utility should not be allowed to cross the line from regulated to unregulated business. The current mess with the telephone companies is an example of the difficulties which can arise when a regulated entity disrupts the competitive marketplace by providing not only its service, but also the related products of that service which can be better supplied by the competitive distribution process. We should not let the energy suppliers disrupt the market for the products currently supplied by competitive suppliers and contractors in the United States.

The proposals offered by the Chief Counsel, Frank Swain, are positive approaches. But they require commitments from the Congress, federal agencies and the states to see that these proposals move beyond this hearing.

Congressman, 15 years ago suppliers testified before the House Small Business Committee because of these very same problems of competition from utilities. I am here today because the problem for small business still exists in even greater force.

I sincerely hope that this hearing need not be repeated in 1998.

Thank you again for affording me this opportunity to appear before you today.

costs less to run, and lasts up to
20 years—or longer?

Appendix "A"

Appendix "A"

TUESDAY, OCTOBER 18, 1983

DAILY TRIBUNE, SEYMOUR, INDIANA



**If you said gas heat,
you're getting warmer.**

A new, high-efficiency gas furnace keeps you comfortably warm while it saves you money. That's the Gas Advantage... the best value for your money.

You can see the savings.

A super efficient gas furnace reduces your fuel consumption by as much as one-third. That's quite a payoff. And these savings are even more significant when you compare them with other heating options.

You feel the difference.

A high-tech gas furnace delivers warm, even heat at all temperatures. And it doesn't require back-up heating equip-

ment when the temperature drops below 30 degrees.

You can count on efficiency.

Year after year.

With a new high-tech gas furnace you save now and in the long run. Your first cost is usually lower. Annual operating costs are lower. Equipment life is longer. And warranties outlast those other systems carry. It's comforting to know that gas gives you more for your money. If you'd like to know more about the Gas Advantage and how it can save you money, just fill out and return the coupon, or call our toll-free number. We'll send you free information.

For more information return this coupon to:

The Gas Advantage
P.O. Box 7055
Indianapolis, IN 46207

Name _____

Address _____

City _____

State _____

Zip _____

Or, call toll-free 1-800-772-7243 (during normal business hours Monday-Friday.)

Get the Gas Advantage. Gas gives you more for your money.



Appendix B

DAILY TRIBUNE, SEYMOUR, INDIANA

TUESDAY, NOVEMBER 2, 1962

Starting This Week...

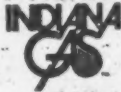
Energy-Efficient gas appliances
with the many "Gas Advantages."

Indiana Gas Company is pleased to announce that starting this week modern gas appliances will be displayed and sold at their Seymour District Office at 509 West 2nd Street. Stop by and see the new generation of energy-efficient gas ranges, water heaters, space heaters, clothes dryers and the popular outdoor gas grills. No other fuel offers household comfort and convenience with the total system efficiency of gas. Efficiency is a "Gas Advantage."

If you plan to replace an appliance or add a new one, let us show you the energy-efficient ones. With prior approval, balance may be added to your gas bill.



Special Introductory Sale Prices on
Gas Appliances



509 West 2nd Street • Seymour • 522-1849

Miami's 12-7 triumph over East Carolina on a touchdown with 1:04 remaining dropped the Hurricanes from fifth to sixth with 961 points.

Southern Methodist, a 20-6 winner over Rice, climbed from eighth to seventh with 815 points.

the 500 mark.

McNorton's intent both came in the form as the Giants try to post their first six games.

All the Giants came on field goals Ali Haji-Sheikh with kicks of 27, 56 and Haji-Sheikh is the first in NFL history to field goals of at least in one season.

Still, it was little the Giants fell to 3-0 the NFC East.

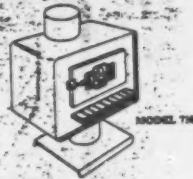
BASEBALL
American League
CLEVELAND II
Named Doc Edwards of their Maine in the International

CONCRETE
Mixed On The
Job. No Waste...
No Over-Run.

POLLEY
Building Supply, Inc.
1200 E. O'Brien 522-0915

The Earth Stove.

NEW
Efficiency at Low Cost



CHECK US OUT:

MORE VALUE PER DOLLAR SPENT
THAN ANY AIR TIGHT STOVE BUILT.

- Automatic Draft Control
- Fire Brick Lined
- Air Tight Construction
- Large Cook Top
- Overnight Burn
- 5 Year Warranty

SEE IT AT:

Central Lumber & Supply Co.
BUILDING MATERIALS & SUPPLIES
10th & Pershing Sts. 522-3326

37-000 172

was maybe the best
at of high school that
s not looking to score.
to score. Several more.

WEDNESDAY, NOVEMBER 9, 1965

SEYMOUR, IN.

Appendix "C"

DAILY TRIBUNE, SEYMOUR, INDIANA

PAGE THREE

planning g format

rather ideas for the year and announce a.

board approved a vision changing the of the executive s, adding two new broader coverage g the names of the them more rep- ra.

live committee now are president, ident, secretary, and chairmen of d, outside events, nd grounds, lives- bition, carnival, ns and inside ex- l and FFA activi- vement's activities n.

d granted permis- H use of the Show scales for its beef

identification program on Jan. 14, with alternate date of Jan. 21.

Three members offered resignations for personal reasons. They are Lester Darlaga, Cliff Osterman and Ed Blush. On behalf of the board, Mrs. Ery expressed appreciation for their time and service to the fair.

Counting the three county commissioners who serve by virtue of their office, the fair board is comprised of 31 members. The membership committee will be meeting soon to present a slate of replacements, probably at the next board meeting at 7:30 p.m. Dec. 8.



INDIANA GAS COMPANY, INC.

Theresa Gabaree has been named Appliance Sales Representative for the Seymour District of the Indiana Gas Company. She can be reached during normal office hours, at the office, 509 W. 2nd Street, 522-1849. The gas company is featuring a line of energy-efficient gas ranges, water heaters, space heaters, clothes dryers and washers, dishwashers and gas grills. The appliances are available on a 30 day cash basis, or can be paid for monthly with a customer's gas bill.

ital

nts of a son.

— Benson, Norman
parent of a

— diemansala
lip G. Miller,
n R6, admitted

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R2, admitted

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St., Vallonia,
1.

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orth Vernon.

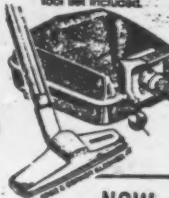
special holiday prices! EUREKA VACS

YOUR
CHOICE!
\$69⁹⁵

4-position Dial-A-Height®
cleans carpeting from low
naps to high shags.

MODEL
1425

Complete 7-piece cleaning
tool set included.



SUGGESTED
LIST \$129.95
MODEL 1481

Exclusive Vibro-Groomer® roller
bar brush roll loosens deep grit and
ground-in dirt.
Brilliant headlight seeks out dirt.
Regulator® sliding scale height
adjustment cleans from low naps
to high shags.



NOW
\$109⁹⁵
SAVE \$20

A motor
here

3 peak HP

TUESDAY, NOVEMBER 15, 1965

SEYMOUR DAILY TRIBUNE, SEYMOUR, IN.

...the group...
...the Rainbow...
...he will perform...
...e direction of Keith...
...al will include ham...
...ans, macaroni and...
...east rolls, salad, de...
...a drink...
...are \$4.50 and may...
...used from any chor...
...student, student...
...member or in the...
...ce until noon Thurs...
...kets will be sold at...
...the doors will open

r plans ior bid

NAPOLIS (AP) —
Republican State
John Snyder says
ormally announce
se is running for the
an nomination for

said Friday he will
announcement dur...
-day sweep of the
gining at 8 a.m...
st the Indianapolis
b...
who lives near Wil...
Hancock County,
state chairman in
early 1972 before
to let James Neal
sville take over...
as elected state
in 1966 and in 1968

ng bill House

NGTON (AP) —
Indiana congress...
in the majority as
passed 224-189 an...
y spending bill to...
of the federal gov...
-running past mid...
sts Katie Hall, Lee...
and Frank McClos...
for the measure...
Burton, R-Ind, did...
in Republicans...
mocrats voted for...
ile 49 Democrats...
epublicans voted

Monday births
Mr. and Mrs. Patrick D.
Barnes, 802 Sprenger Road,
are the parents of a daughter.

Mr. and Mrs. William Hen...
drix, Commiskey Rt. 1, are the
parents of a son.

Monday dismissals
Mrs. Alma E. Schulz,
Lutheran Community Home,
admitted Oct. 30.

Guy R. Robertson, Brown...
stown Rt. 1, admitted Nov. 7.

Treated wood fuel dangerous

INDIANAPOLIS (AP) —
Hoarders who use chemically
treated wood to heat their
homes risk being poisoned by
toxic substances released
during the burning, Gov.
Robert D. Orr's energy
adviser says.

Orr aide Charles Coffey re...
ferred to wood marked,
"Treated with chromate...
copper-arsenate (CCA)" or
"For below-ground use."

Recently, a rural family of...
eight who heated their home...
with a stove fueled with let...
treated wood and plywood had sym...
ptoms of copper, chromium
and arsenic poisoning, he
said.

Symptoms included bron...
chitis, pneumonia, ear infec...
tions, blackouts, stomach
and intestinal ailments,
nosebleeds, muscle cramps
and rashes on the arms, legs
and soles of the feet, Coffey
said.

Similar poisoning could...
occur in other homes where
treated wood is burned fre...
quently, he said. "Don't
take a chance. Send your tre...
ated wood scraps to the gar...
bage can."

The Natural Choice...

Natural Gas Water Heaters!

Gas heats water twice
as fast for approximately
half the cost — saving
time and energy.



SALE

A.O. SMITH
and
RUUD

Water Heaters

30 gallon

Ruud RP-30

or

A.O. Smith KGA-30

Sale \$189.50

40 gallon

Ruud RP-40

or

A.O. Smith KGA-40

Sale \$199.50

(Prices good through 11/30/65)

COST MAY BE ADDED TO YOUR GAS BILL

(Delivery and Installation Available)

INDIANA
522-1849
509 W. 2nd Street

37-000 174

Sylvia Patrick, hostess...
at 1 p.m. Dec. 13 at Ruid's...
dinner with the Alpine Club...
The next meeting will be a

fund...
Sylvia Patrick, first vice...
president, presided...
donated \$100 to the nursery



The Natural Choice For Double Savings!

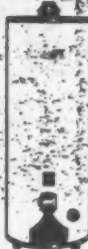
Efficient natural gas appliances
with the "Gas Advantage"
Now at special holiday savings



1. Save from \$40.00 to \$50.00 on Kelvinator and Whirlpool washers and gas dryers
2. Dry your clothes faster for less than half the cost



1. Save up to \$20.00 on quality energy efficient gas water heaters
2. Save energy dollars — gas heats water twice as fast at approximately half the cost



1. Save from \$40.00 to \$60.00 on modern energy efficient gas ranges
2. Save 25% to 30% on energy costs when you cook with gas

Only gas gives you smokeless broiling — 1001 temperature settings — Instant on, instant off



(Prices good through 12/31/83)
COST MAY BE ADDED TO YOUR GAS BILL
(Delivery and Installation Available)



522-1849

509 W 2nd Street

Apparatus
DAILY TRIBUNE, SEYMOUR, INDIANA

TUESDAY, DECEMBER 20, 1983

The Natural Choice For Double Savings!

Efficient natural gas appliances
with the "Gas Advantage" . . .
Now at special new year savings



1. Save from \$40.00 to \$50.00 on Kelvinator and Whirlpool washers and gas dryers
2. Dry your clothes faster for less than half the cost

1. Save up to \$20.00 on quality energy efficient gas water heaters
2. Save energy dollars — gas heats water twice as fast at approximately half the cost

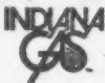


1. Save from \$40.00 to \$80.00 on modern energy efficient gas ranges
2. Save 25% to 30% on energy costs when you cook with gas

Only gas gives you smokeless broiling — 1001 temperature settings — Instant on, Instant off



(Prices good through 1/31/84)
COST MAY BE ADDED TO YOUR GAS BILL
(Delivery and Installation Available)



522-1849

509 W. 2nd Street

Appendix
F.1
DAILY TRIBUNE, SEYMOUR, INDIANA

TUESDAY, JANUARY 10, 1984

Appendix G

SEYMOUR DAILY TRIBUNE, SEYMOUR

TUESDAY, FEBRUARY 7, 1984

The Natural Choice For Double Savings!

Efficient natural gas appliances
with the "Gas Advantage"
Now at special February savings



1. Save from \$40.00 to \$50.00 on Kelvinator and Whirlpool washers and gas dryers
2. Dry your clothes faster for less than half the cost

1. Save up to \$20.00 on quality energy efficient gas water heaters
2. Save energy dollars — gas heats water twice as fast at approximately half the cost



1. Save from \$40.00 to \$60.00 on modern energy efficient gas ranges
2. Save 25% to 30% on energy costs when you cook with gas

Only gas gives you smokeless broiling —
1001 temperature settings — Instant on,
Instant off

(Prices good through 2/29/84)
COST MAY BE ADDED TO YOUR GAS BILL
(Delivery and Installation Available)



522-1849

509 W. 2nd Street

night, a 3,032.

Pam McKinney leads the all events scratch (1,569) and handicap (1,881) lists.

Tournament director Anne Baxter said no tournament bowling is scheduled today, but eight teams and 15 sets of doubles will bowl Wednesday morning, beginning at 9:30 o'clock.

ner Beverly LeBrun, Terisa Schwartz, Judy Gambrel, Judy Smith-Sue Nidreth, Roberta Stringer-Mariann Back, June Lucas-Mable Quinn, Carolyn Kruger-Pat Lummelink, Virginia Greene-Phyllis Casady.

Tournament Leaders

Singles: Kathy Allen 943.
Doubles: Pam McKinney-Wanda Thompson 1,247.

Team-Sciara Cleaners 3,026, Bev's Team 3,022, ITT 3,020, Vick's Liquors 2,980, Mary's Team 2,973.

All events-scratch: Pam McKinney 1,569, handicap: Pam McKinney 1,881, Margie Thompson 1,811, Judy Davis 1,801, Cindy LaMarr 1,780, Senja Uhrey 1,747.

Seymour Regional a week ago, had 57 points.

Jennings County placed ninth with 33 points, and Rushville, second to Floyd Central in the regional, was 10th with 29½ points.

Team points (top 10): Evansville Mar-
ter Dei 67½, Indianapolis Roncalli 70,
Floyd Central 57, Mooreville 48, De-
catur Central 40½, Perry Meridian 40,
Bloomington North 37, Ben Davis 34,
Jennings County 33, Rushville 29½.

The Natural Choice...

Natural Gas Water Heaters!

Gas heats water twice
as fast for approximately
half the cost — saving
time and energy.

SALE

A.O. SMITH and RUUD

Water Heaters



30 gallon

Ruud RP-30

or

A.O. Smith KGA-30

Sale \$179.50

(Prices good through 3/31/84)

COST MAY BE ADDED TO YOUR GAS BILL

(Delivery and Installation Available)



40 gallon

Ruud RP-40

or

A.O. Smith KGA-40

Sale \$189.50



522-1849

509 W. 2nd Street

DAILY TRIBUNE, SEYMOUR, INDIANA

TUESDAY, FEBRUARY 14, 1984

Appendix "H"

Don't let winter freeze your water heater. Get a new one now while you can. Our contract is in place and our contract is in place. For more information

mid-winter price break!

Appendix "I"

CHOICE OF TWO MANUFACTURERS

Don't let winter freeze your water heater. Get a new one now while you can. Our contract is in place and our contract is in place. For more information



- **SAVE ENERGY**

Gas heats water twice as fast for half the cost

- **SAVE MONEY**

Up to \$34.00 when you replace your old water heater with a new Ruud or A.O. Smith gas water heater

- **5-YEAR Conditional Warranty against leaking**

*note: 189.50
delivery + install 55.60
245.10*

Delivery and Installation Available
Costs may be added to your Gas Bill.



Either 30 or 40 Gallon

RP30B

Reg. \$209.50

Sale \$179.50

RP40B

Reg. \$223.50

Sale \$189.50

KGA30

Reg. \$201.50

Sale \$179.50

KGA40

Reg. \$220.50

Sale \$189.50

*Interest is 9.9 first year
if can write contract for 1 year
if fail in 90 days there is no INDIANA
interest charged - 1/2 written for 1/2
1 yr on days and paid 1/2 early interest for
remaining time is subtracted (you pay interest only on time in which payment are made)*

1 yr. — 23.57 month
2 yr. — 12.85 month
3 yr. — 9.15 month

Sales Representative

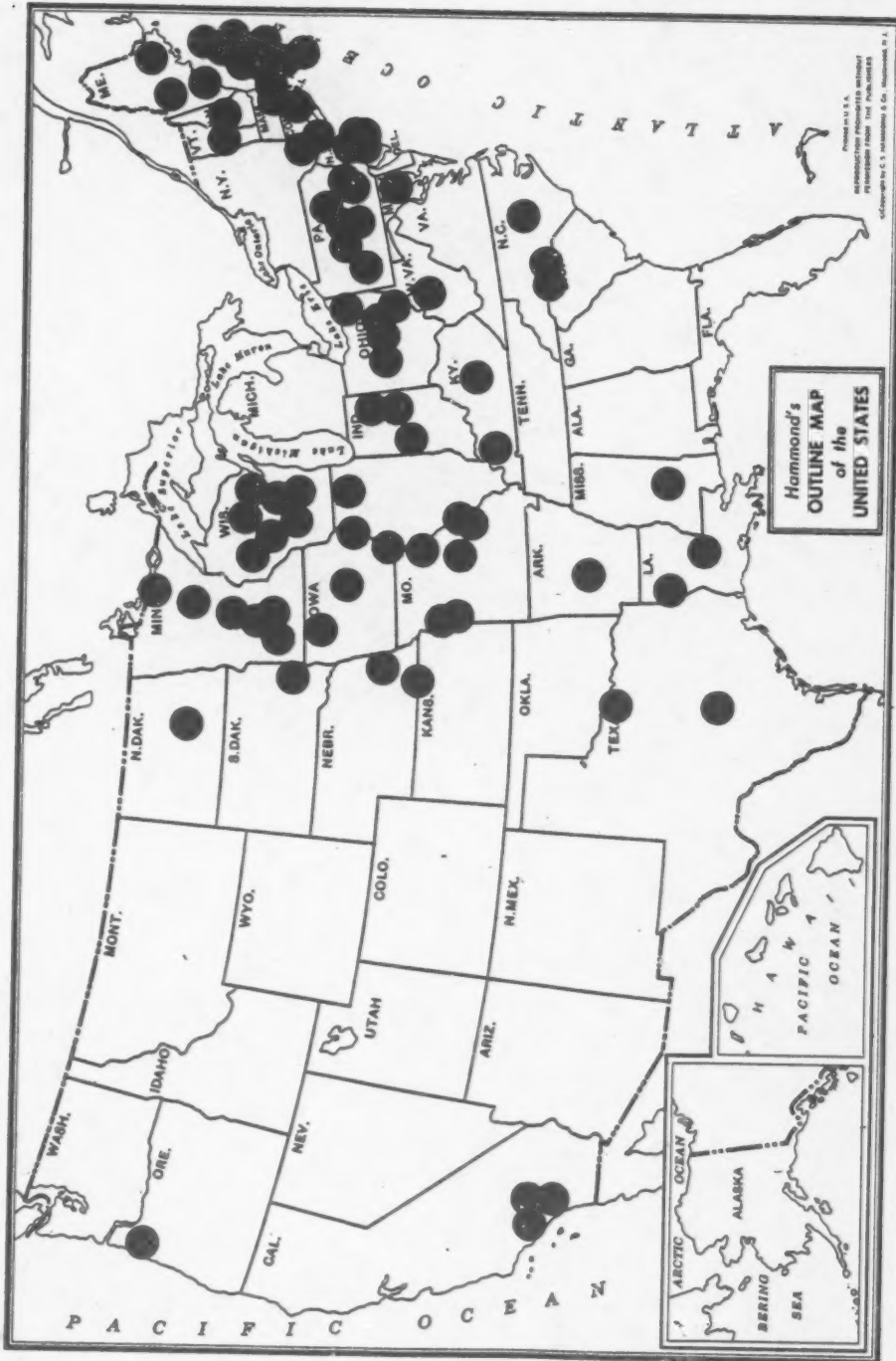
Phone

Appendix "J"



THERESA GABAREE
Sales Representative

INDIANA GAS COMPANY, INC.
509 W. 2nd Street
Seymour, IN 47274
Bus.: 812-522-1849
Res.: 812-346-1564



GAS AND ELECTRIC UTILITIES IN DIRECT COMPETITION WITH SUPPLIERS *Arkansas

Arkansas - Louisiana Gas

California

Southern California Gas Company

Edison Company

Department of Water and Power

Connecticut

Connecticut Light & Power

Illinois

Northern Illinois Gas

Iowa - Illinois Gas & Electric

Wisconsin Power & Light Company

Indiana

Indiana Gas

Northern Indiana Public Service Co. (NIPSCO)

Indiana Power & Light (IP&L)

Iowa

Iowa Electric Light & Power Company

Northern Natural Gas

Keokuk Gas Company

Iowa - Illinois Gas & Electric

Great River Gas Company

Kentucky

West Kentucky Gas

CIPS

Kansas

Kansas - Nebraska Natural Gas Company

Kansas Gas & Electric

Kansas Power & Light

Louisiana

Entex Gas

Arkansas - Louisiana Gas

Maine

Maine Public Service Company

Bangor Hydro Electric

Northern Utilities

Maryland

Baltimore Gas & Electric

* Identified by ASA Survey of its members

(continued)

GAS AND ELECTRIC UTILITIES IN DIRECT COMPETITION WITH SUPPLIERS *Massachusetts

Commonwealth Gas
 Massachusetts Electric
 Cape Cod Gas
 Commonwealth Electric
 Berkshire Gas Company
 Bay State Gas Company
 Boston Gas Company
 Lowell Gas Company
 Fall River Gas Company
 Valley Gas Company
 Eastern Edison Electric

Minnesota

Minnegasco
 Minnesota Natural Gas
 Minnesota Power & Light
 Peoples Gas
 North Central Public Utility
 Ruenstone Electric

Missouri

LaClede Gas
 Union Electric
 Great River Gas Company
 Kansas Power & Light
 Missouri Public Service Company
 Kansas Gas & Electric

Nebraska

People's Natural Gas Co.
 Kansas - Nebraska Gas Co.

New Hampshire

Concord Natural Gas

New Jersey

Public Service Electric & Gas
 Elizabethtown Gas Company
 New Jersey Natural Gas Co.
 P.S.E. & G

New York

Brooklyn Union
 Consolidated Edison

North Carolina

Public Service Co. of North Carolina
 Piedmont Natural Gas
 Duke Power Company

* Identified by ASA Survey of its members

(continued)

GAS AND ELECTRIC UTILITIES IN DIRECT COMPETITION WITH SUPPLIERS *North DakotaMontana Dakota UtilitiesOhio

East Ohio Gas Company

Columbia Gas Company

Ohio Edison

Ohio Gas Company

Buckeye Rural Electric Company

OregonNorthwest Natural Gas CompanyPennsylvaniaU.G.I.

National Fuel Distribution Corp.

People's Natural Gas Company

Philadelphia Gas Works

Philadelphia Electric Company

Pennsylvania Fuels

Pennsylvania Gas & Water

South CarolinaPiedmont Natural Gas

Duke Power

South DakotaMinnegascoTexasLone Star Gas CompanyVermontCentral Vermont Public ServiceWest VirginiaBuckeye Rural ElectricWisconsinWisconsin Gas

Wisconsin Electric

Wisconsin Natural Gas

Wisconsin Fuel & Light

Wisconsin Public Service Co.

WICOR

Wisconsin Power & Light

Madison Gas & Electric

* Identified by ASA Survey of its members

Mr. LUKEN. Mr. Hager.

Mr. WEBER. Mr. Chairman, could I just interrupt for a minute to say that Mr. Hager is a friend from Minnesota and I think, as such, deserves some special recognition. So I just wanted to introduce him to the committee.

Although he is not a constituent of mine, he is a few blocks away and is ably represented by our colleague, Mr. Penny.

We welcome you to Washington.

Mr. HAGER. Thank you, Mr. Weber.

Mr. WEBER. Thank you, Mr. Chairman.

Mr. LUKEN. Mr. Hager, you may proceed with that auspicious introduction.

TESTIMONY OF HAROLD J. HAGER, PRESIDENT, FARM & GUSTAFSON PLUMBING AND HEATING, INC., AND MEMBER, NATIONAL ASSOCIATION OF PLUMBING-HEATING-COOLING CONTRACTORS

Mr. HAGER. Good afternoon, Mr. Chairman. Thank you for giving us this opportunity to testify.

My name is Joe Hager, and I am president of Farm & Gustafson Plumbing and Heating, Inc., of Mankato, MN.

We do plumbing and heating work with an annual volume of about \$700,000. Our work force has dropped from seven to four mechanics, in part due to unfair competition from our gas utility, Minnegasco.

I am president of the Plumbing-Heating-Cooling Contractors of Mankato and a past president of the Plumbing-Heating-Cooling Contractors of Minnesota. I am here today representing the National Association of Plumbing-Heating-Cooling Contractors.

Mankato is a community of a little over 38,000 people in southern Minnesota. Our gas utility is Minnegasco.

I strenuously object to the unfair and anticompetitive practices of the utility through their involvement in service work and in sales and installation.

My business has already been seriously injured. Although I do both plumbing and heating work, the utility has taken away practically all of my heating service business in Mankato.

Minnegasco offers the consumers a plan known as service plus, also described as maxi-policy. The utility will provide a service contract for \$5.95 per month. This contract covers labor and materials for service to the furnace, boiler, gas stove, gas dryer, gas water heating, and gas grill. They also cover electrical appliances including electric ranges, dryers, and water heaters. The chart enclosed in my written testimony verifies that.

The utility has also negotiated service contracts with bigger commercial establishments. For example, they have contracts to maintain the rooftop heating and air-conditioning units at two Holiday Inns, Cotter Co., and the Madison East Shopping Center.

Minnegasco also sells and installs their own equipment, including boilers, gas furnaces, gas grills, gas space heaters, gas dryers, and gas water heaters, as well as ventilation and attic insulation. To support their sales effort, they operate an appliance store in the mall in downtown Mankato.

There is a newspaper ad enclosed that they recently ran in Minnegasco centers.

I, too, run an appliance store approximately 2½ blocks from the mall. My shop sells water heaters, boilers, disposals, and dishwashers.

Recently I had a job installing the gas piping for the Islander Restaurant. However, the utility brought in the appliances and hooked them up. I didn't even get a shot at bidding the work.

The real competition problems come from the tremendous marketing advantages which the utility enjoys, using its protected monopoly status.

Financing and credit information. Minnegasco offers 12 percent financing. Moreover, they have builtin credit information from the records of the gas billings. They even provide a zero financing charge up to 90 days. The best I can offer is 16 percent on a 90-day financing. Otherwise, my customers can charge on their VISA card for long-term financing at about 18 percent.

No. 2, billing. Minnegasco can place the cost on the gas bill. They have little additional billing costs since the ratepayers are paying for all that, including envelopes and postage, as part of the gas rates.

No. 3, use of name. Minnegasco's name is a valuable asset in sales, installation, and service. Our telephone directory business listings provide an excellent example. Not only does Minnegasco offer both emergency answering service 24 hours, but also 24-hour appliance sales, and both have the same number. If your water heater blows up, they are right there to sell you a new one.

No. 4, advertising. Minnegasco regularly uses their bills for bill stuffers, promoting the sale of its boilers, furnaces, water heaters, and other equipment. Postage is apparently paid by the ratepayers. The utility also uses newspaper ads, radio, and television to communicate their marketing messages, using Minnegasco's name.

Clearly, I can't get free postage or include a mailing with the utility's bills to promote the products I sell.

No. 5, direct mail. Minnegasco has up-to-date mailing lists of all gas consumers for direct mail access. Here is their service contract offer which I recently received. That's included in that.

Normally, I would sell and install between six and eight replacement boilers per year. Minnegasco has unfairly stolen that business away. Last year, I didn't sell a single one in Mankato. My only boiler business was limited to two that we put in beyond the city limits.

Utilities have an inherent competitive advantage. Utilities are large businesses with protected status provided by the State public utility commissions. Contractors are small businesses who compete vigorously to even make a profit.

We already have seen the growth in the utility activity and markets that have traditionally been the contractor's. Under existing law, utilities are stealing our markets.

Contractors and their mechanics are highly skilled and technically competent people. Normal requirements for plumbers are 4 years of classroom and on-the-job apprentice training to become a journeyman and up to 10 years as a journeyman to apply for a master plumber's license and work as a contractor.

Two-thirds of the States have licensing laws to ensure competency for plumbing contractors. Many of the remaining jurisdictions have local licensing laws. These requirements have been developed to protect the health and safety of the consumer.

During the last few years, there has been a great deal of public attention to developing public policy that promotes the health and viability of small business. However, even the larger contractors are finding that they are no match to the vast array of resources available to utilities.

There are usually a number of contractors in an area. Although we compete vigorously, few have the capability to approach the name recognition of a utility, because we do not have the same opportunities for comprehensive regular contact with consumers.

If a utility takes over this work, the injury is not only to the small business contractors but also to the thousands of skilled mechanics they employ and to consumers, who will find that there are less alternatives to choose from. Competition will have been eliminated.

As evidenced by our problem with competition with Minnegasco, this is not theoretical. The market disruption has already begun, whether it be gas grills, water heater sales, or other repair services.

In a recent survey of the National Association of Plumbing-Heating-Cooling Contractors members, 50 percent responded they were being adversely affected by utility competition. Only 3 percent found that their business is greatly enhanced by utility practices. This is despite utility claims that they are attempting to create new markets which would benefit contractors.

What is unfortunate is the large number of small businesses that are unable to seek relief because of the large amount of time, effort, and money necessary to pursue it.

In some States, utilities have used their staying power and ratepayer-financed attorneys to drag out and outlast underfinanced contractor legal efforts.

While we hoped that the State regulatory commissions would stem the tide of the utility growth, that has generally not been the case. The commissions have focused on energy conservation and have not yet been concerned with looking at the competitive impact, particularly on small business. In fact, in one State—New York—the public service commission specifically rejected the State Attorney General's request that competition be considered.

In conclusion, small business contractors are being forced to support their competition. Since utilities are monopolies and are the sole source for gas or electric service, contractors must pay the rate set by the utility, which includes utility costs to run their nonutility programs.

Contractors are already facing increased utility competition in many parts of the country. Because of the competitive imbalance and the utilities' monopoly control of resources, we believe that there already is a serious problem of unfair activity by utilities.

We support the recommendations made by the Alliance for Fair Competition. Utilities should be prohibited from sales and service and installation. If the antitrust laws need to be strengthened to prevent anticompetitive marketing practices, let's do so.

By all means, let's not promote the problem through the conservation programs. Let's provide energy conservation through the competitive marketplace and prohibit utilities from taking unfair advantage of these programs.

We urge Congress to move quickly to adopt solutions which will prevent utilities from abusing customers through cross-subsidy, which will preserve a fair, competitive environment for small business.

Thank you very much.

[Mr. Hager's prepared statement with attachments follows:]

PREPARED STATEMENT OF HAROLD J. HAGER, PRESIDENT, FARM AND GUSTAFSON PLUMBING AND HEATING, INC., AND MEMBER, NATIONAL ASSOCIATION OF PLUMBING-HEATING-COOLING CONTRACTORS

Good afternoon, Mr. Chairman. thank you for scheduling these hearings and for giving us this opportunity to testify on unfair and anticompetitive practices by utilities. Certainly, the utility in my area has an unfair competitive advantage and serves as an example of the types of problems small business is experiencing around the country.

My name is Harold "Joe" Hager and I am President of Farm and Gustafson Plumbing and Heating, Inc. in Mankato, Minnesota. We do plumbing and heating work with an annual volume of \$700,000. Our work force has dropped from 7 to 4 mechanics in part due to unfair competition from our gas utility, Minnegasco.

I am president of the Plumbing-Heating-Cooling Contractors of Mankato and a Past President of the PHCC of Minnesota. I am here today representing the National Association of Plumbing-Heating-Cooling Contractors. Accompanying me are Charles Lavin and Dennis LaValle of our national staff.

The National Association of Plumbing-Heating-Cooling Contractors (NAPHCC) is the oldest national association in the construction industry and the largest in the plumbing-heating-cooling industry. It has 6000 members, small businessmen who thrive on open and fair competition. Membership comes from every state in the country and is organized through about 300 state and local affiliated associations. This industry employs over 450,000 people and has receipts of over 32 billion dollars.

Mankato is a community of a little over 38,000 people in southern Minnesota. Our gas utility is Minnegasco. As a consumer and as a businessman, I strenuously object to the unfair and anticompetitive practices of the utility, through their involvement in service work and in sales and installation.

My business has already been seriously injured. Although I do both plumbing and heating work, the utility has taken away practically all of my heating service business in Mankato.

Minnegasco offers consumers a service contract known as "Service Plus." Also described as their "Maxi-Policy," the utility will provide a service contract for \$5.95/month. This contract covers labor and materials for service to the furnace or boiler, gas stove, gas dryer, gas water heater, and gas grill. They also cover electric appliances including electric ranges, dryers and water heaters. Attachment A is a chart describing the coverage.

The utility has also negotiated service contracts with bigger commercial establishments. For example, they have contracts to maintain the rooftop heating and air conditioning units on the Holiday Inn, Cotter Company, and the Madison East Shopping Center.

Minnegasco also sells and installs their own equipment, including boilers, gas furnaces, gas grills, gas space heaters, gas dryers and gas water heaters as well as ventilation and attic insulation. To support their sales effort, they operate an appliance store in the Mall in downtown Mankato. Attachment B is a newspaper ad they ran recently for their Minnegasco Center.

I, too, run an appliance store. Approximately 2½ blocks from the Mall, my shop sells water heaters, boilers, disposals and dish washers.

Recently, I had a job installing the gas piping for the Island Restaurant. However, the utility brought in the appliances and hooked them up. I didn't even have a shot at bidding the work.

So where's the unfair competition, you may be asking. It is in prices? On the whole, their prices appear to be competitive. However, price may still be a concern if all of their indirect costs are not included.

The Minnesota Public Utilities Commission examined Minnegasco's pricing structures in 1981 based on complaints from contractors that utility services were being subsidized. For 1980 expenses of \$12.7 million for service work, rate payers subsidized \$8.5 million. The Commission concluded "that all rate payers should not bear the burden of the company's customer appliance service expenses. Rather those who use the service should bear the cost."¹

We have not examined the accounting to determine how indirect expenses such as administration and overhead are covered. However, as my testimony will indicate further, I doubt that these other costs have been included.

No, the real competition problems come from the tremendous marketing advantages which the utility enjoys using its protected monopoly status:

1. Financing and credit information—Minnegasco offers 12% financing. Moreover, they have built in credit information from the records of the gas billings. They even provide a zero financing charge for up to 90 days. The best I can offer is 16% on 90 day financing. Otherwise, my customers can charge it on their Visa card for longer term financing at about 18%.

2. Billing—Minnegasco can place the cost on the gas bill. They have little additional billing costs since the rate payers are paying for all of that including envelopes and postage as part of the gas rates. Billing costs are one of my costs of running my company.

3. Use of name—Minnegasco makes full use of its company name in its sales, installation and service. Everyone in Mankato knows Minnegasco. That instant name recognition is a valuable asset of its monopoly gas operations which the utility uses to promote its other business activities.

The green pages (equivalent to the yellow pages in many other communities) provides an excellent example (See Attachment C). Not only does Minnegasco offer both "Emergency Service (Answered 24 hours)" but also 24 hour "Appliance Sales"—and both at the same phone number! If your water heater blows up, they're right there to sell you a new one.

4. Advertising—Minnegasco regularly includes bill stuffers promoting the sale of its boilers, furnaces, water heaters and other equipment. Postage is apparently paid by rate payers. The utility also uses newspaper ads, radio and television to communicate their marketing messages using the Minnegasco name. I don't know whether some or all of those expenses are charged to rate payers or included in the expenses of carrying out their businesses.

Clearly, I can't get free postage or include a mailing with the utility's bills to promote the products I sell. As a small businessman in an unregulated market, I can't charge all consumers in the area for my advertising. I include it as part of my overhead which I charge only to my customers.

5. Direct mail—Minnegasco has the up-to-date mailing lists of all gas consumers for direct mail access (See Attachment D). They have the capability to update them regularly from their direct involvement with new and terminated customers. That kind of current list isn't even available to me. Even a less accurate list would only be available at commercial mail list rates.

Normally, I would sell and install 6 to 8 replacement boilers per year. Minnegasco has unfairly stolen that business away. Last year, I didn't sell a single one in Mankato. My only boiler business was limited to two that we put in beyond the city limits.

UTILITIES HAVE AN INHERENT COMPETITIVE ADVANTAGE

Utilities are large businesses guaranteed the opportunity for a rate of return by the state public utility commissions.

Since the rate of return is set by the state regulatory commission, the utility must turn to increasing its investment which provides a larger rate base to enable it to increase profits. This, in turn, produces higher rates to the consumer.

Contractors are small businesses who compete vigorously to even make a profit. We already have seen growth in utility activity in markets that have traditionally been the contractor's. Under existing law, utilities are stealing our markets.

The competition created by the utility may result in lower direct costs to the consumer in the short term. However, this hides the indirect costs. Overhead and administration are hidden in the rates paid for by all rate payers.

As recently as the beginning of the last decade, utilities were aggressively promoting energy consumption to enhance revenues and investment. With the onset of the energy crisis in the mid 70's, utilities sought new means to compensate for declining

¹ Minnesota Public Utility Commission, PUC Docket No. G-008/GR-82-249, August 27, 1981.

revenues. In the disguise of promoting energy conservation, they continue to promote energy consumption. They do this through the promotion of new energy consuming equipment and through fuel switching.

Utilities already had some involvement in service work. These efforts are now extending to sales and installation as well. As utilities establish reputations for contracting services, they enhance their ability to branch out.

The National Energy Conservation Policy Act (NECPA) prohibits utilities from sales, service and installation of energy conservation measures unless they were already involved in these activities prior to enactment. We have already seen many new initiatives to compete with contractors by those utilities that were grandfathered under NECPA.

HOW UTILITIES DESTROY COMPETITION IN NON-UTILITY MARKETS

Contractors and their mechanics are highly skilled and technically competent people. Normal requirements for plumbers are 4 years of classroom and on the job apprentice training to become a journeyman and up to 10 years as a journeyman to apply for a master plumber's license and work as a contractor. Two thirds of the states have licensing laws to insure the competency of plumbing contractors. Many of the remaining jurisdictions have local licensing laws. These requirements have been developed to protect the health and safety of the consumer, yet many utilities do not operate under the same requirements.

Practically all of the members of the National Association of Plumbing-Heating-Cooling Contractors are small businesses by standards set by the Small Business Administration. The median contractor nationwide grosses less than half a million dollars annually and employs about 6 mechanics.

During the last few years, there has been a great deal of public attention to developing public policy that promotes the health and viability of small business. However, even the larger contractors are finding that they are no match to the vast array of resources available to utilities.

Let me cite some examples.

Utilities can hire marketing, publicity, economic and technical experts to develop messages to the consumer. They can target efforts at particular products. The small business contractor cannot afford the overhead to develop these sophisticated marketing tools.

They can negotiate favorable prices through bulk orders directly with manufacturers. A contractor purchases products for installation from his supply house who in turn obtains them from the manufacturers.

Utility companies have direct mail access (with postage paid for by the rate payer) into the homes of consumers via enclosures with regular utility bills. Small business contractors must cultivate every lead they get.

Utilities benefit from cross-subsidization by all rate payers, some of it mandated by statute to perform the Residential Conservation Service energy audits under NECPA. Small business contractors must collect all of their costs for a job from that customer. Certainly contractors are in no position to offer rebates as utilities have done.

Whether marketing through a subsidiary or directly, customer credit checks can be made readily by the utility by checking the payment record on utility bills. Such readily available credit checks are not as available to small business contractors.

Utilities frequently have financing programs at favorable interest rates for consumers. The consumer may be able to make payments on utility contracting measures over an extended period of time as part of the utility bill. Small business contractors seldom have the capital or cash flow to provide such financing arrangements.

When utilities or their subsidiaries expand or develop new promotional practices, risk plays a different role. If they lose money, they still have the rate base to fall back on. A small business contractor who seeks to expand or develop new markets may find it necessary to risk the whole company with no parent operations to fall back on.

By their very nature as publicly regulated businesses, utilities are monopolies that reach into most homes and businesses in the service area. Signs and markers designate the presence of their facilities and remind us of their network. Every month, we see their bill come in. Every month, we are reminded of the name of the utility when we write our check. Thus, whether they sell, install or service equipment on their own or whether they do so through a subsidiary, they have an immediate advantage of name recognition before they even print their first advertisement.

In contrast, there are usually a number of contractors in an area. Although we compete vigorously, few have the capability to approach the name recognition of the utility because we do not have the same opportunities for comprehensive regular contact with consumers.

If the utility takes over this work, the injury is not only to the small business contractors, but also to the thousands of skilled mechanics they employ, and to consumers who will find they have less alternatives to choose from. Competition will have been eliminated.

ENERGY MARKET IS ONE TARGET

The threshold for major penetration of this market has already been crossed. The risk of monopolization of the energy conservation market has probably never been greater.

The best example is the requirement that utilities offer and subsidize the energy audit. Those small businesses who once made a living from this market are no longer able to do so. Based on a Michigan court decision, they are even precluded from relief under the antitrust laws.

Sales of energy conservation products is another major area. Licensing requirements and other state and local regulations assure consumers of the integrity of contracting firms. Yet some utilities are using only selected contractors. The use of this practice institutionalizes a market allocation scheme.

If utilities emphasize the sale of equipment, leaving the installation to contractors, then the contracting industry loses its independent and competitive character and becomes beholden to them for business. The utility is able to determine prices and to enter the ranks of brokers of contracts. If the utilities pursue the installations as well, then many small business contractors will be left bankrupt in the trail of growing utility dominance.

In addition, contractors face even greater threat on the horizon. With the passage of the Energy Security Act in 1980, Congress created the Commercial and Apartment Conservation Service (CACS). Under this program and under regulations just released from the Department of Energy implementing it, there are no protections whatsoever against anticompetitive activity. As soon as state plans under the CACS go into effect, utilities will be required to provide energy auditing services to apartment buildings and small commercial enterprises. We expect to see a major increase in promotional practices in sales, service, and installation by the utility companies throughout this country, as they take advantage of this federally provided marketing opportunity.

DISRUPTION OF OTHER MARKETS HAS BEGUN

As evidenced by our problem with competition from Minnegasco, these are not theoretical possibilities. The anticompetitive practices are there. The market disruption has already begun, whether it be gas grills, water heater sales or other repair services.

In a recent survey of NAPHCC members, 50% responded that they were being adversely affected by utility competition. Only 3% found their businesses greatly enhanced by utility practices. This is despite utility claims that they are attempting to create new markets which would benefit contractors.

The files grow daily with new reports of new programs and anticompetitive practices by more utilities. Individual contractors and contractor associations are challenging these before the public service commissions and in the courts. Detailed examples have been provided to the committee staff.

While there have been some notable successes, there have been disastrous losses. Certainly, the refusal of one state commission to even conduct a hearing would fall in the latter group.

What is even more unfortunate is the large number of small businesses that are unable to seek relief because of the large amounts, of time, effort and money necessary to pursue it. In Connecticut and North Carolina and other states, utilities have used their staying power and rate payer financed attorneys to drag out and outlast underfinanced contractors legal efforts.

Utilities have already made major inroads in the sale, installation and service of equipment which traditionally belonged to the contractor. As an appendix to my testimony, I have attached some of examples of these intrusions into our markets (Appendix E). I understand that our staff has supplied the subcommittee with a great deal of material on practices by a number of utilities.

In a recent survey of the NAPHCC membership, 45% have already experienced sales and installation of gas fired appliances by utility companies. In addition, more than half of the contractors agreed that utilities offer an unfair price advantage.

While we would hope that the state regulatory commissions would stem the tide of the utility growth, that has generally not been the case. As in reports from Florida and in New York, the commissions have focused on energy conservation and have not been concerned with looking at the competitive impact, particularly on small business. In fact, in the Long Island Light Company case in New York, the Public Service Commission specifically rejected the state Attorney General's request that competition be considered.

RECOMMENDATIONS

(1) Our experience indicates that attempting to save our businesses by combating utilities on their turf is extremely difficult. We don't have the resources to examine their cost allocations thoroughly. Many public service commissions don't either. It would be far more practical to simply prohibit utilities from sales, service, installation or rental practices on the house side of the meter.

(2) Alternatively, if utilities are permitted in, the law should allow these programs only if offered at fully compensatory market based rates after public hearings on the effect on competition. We recommend that the standards identified by the Chief Counsel for Advocacy in his March, 1984 report on "Utility Competition with Small Business" be used. In this way, the nonregulated activities will pay their full share, thus permitting the utility to save on its utility costs. These savings can be passed on to the rate payer.

(3) The antitrust laws, and particularly Federal Trade Commission authority should be expanded to fully address unfair competition not only through predatory pricing, but also through marketing practices of utility monopolies. There will continually be new competitors for the utilities. Yet the goal of this committee and of small business programs has been to promote stability and growth of small businesses. Contractors are less likely to devote their full resources to their businesses if they constantly face the risk of being thrown out of business by utility practices.

(4) Relief must be made more readily available. A small business cannot thrive and grow while constantly being forced to fight for survival. We should be able to obtain quick and fair consideration by our state regulatory bodies. However, relief should also be readily available through the FTC, or the Justice Department particularly when states fail to act or lack authority.

(5) The Residential Conservation Service (RCS) and the Commercial and Apartment Conservation Service (CACS) should either be repealed or be amended to provide strong anticompetitive protections. Thus, our organization has been seeking competition amendments to H.R. 5467, a bill by Rep. Richard Ottinger that would reform those programs. If effective amendments are not included, we have no choice but to continue to oppose these programs which give federal encouragement to unfair utility competition.

CONCLUSION

Small business contractors are being forced to support their competition. Since utilities are monopolies and are the sole source for gas or electric service, contractors must pay the rates set by the utility, which includes utility costs to run their non-utility programs.

Contractors are already facing increased utility competition in many parts of the country. Because of the competitive imbalance, such as cross subsidization, and the utility's monopoly control of resources, we believe that there already is a serious problem of unfair and anticompetitive activity by utilities.

We urge the Congress to review our recommendations and move quickly to adopt solutions which will prevent utilities from abusing consumers through cross-subsidization and which will preserve a fair competitive environment for small business.

Thank you and I would be happy to answer any questions.

STOP BURNING MONEY

Attachment B

Cut Your Fuel Use
as Much as 33% with a
New Gas Heating System.

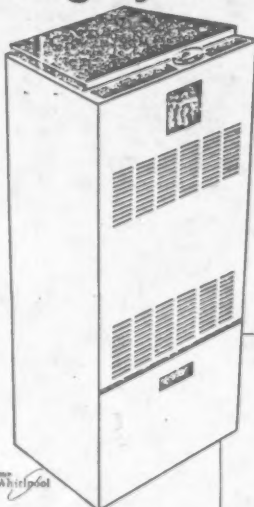


On Sale at
Minnegasco Centers.



A new generation of high technology gas heating systems. They're the right choice for your home heating needs because you may be able to cut your fuel consumption by up to one-third.

If your present heating system is six years old or more, it is probably operating at an Annual Fuel Utilization Efficiency (AFUE) of less than 65%. But the new super-efficient systems have an AFUE rating of over 80%—as much as 96% with the Whirlpool TightFist II.



Whirlpool TightFist II™ Gas Furnace up to 96% Efficient.

Combines state-of-the-art energy-saving technology with the proven reliability of a Whirlpool furnace. Operates quietly and efficiently to give you warm comfort for years to come. Twenty-year warranty on the heat exchanger.

The higher the AFUE, the more energy and money you save!

ENERGY SAVINGS CHART LOWER EFFICIENCY EQUIPMENT

	GAS HEAT 65% AFUE		GAS HEAT 70% AFUE	
	CCF/YR ¹	COST/YR ²	CCF/YR ¹	COST/YR ²
Example 1	980	\$578	910	\$517
Example 2	1200	\$708	1114	\$637
Example 3	1400	\$826	1300	\$767

HIGHER EFFICIENCY EQUIPMENT

	GAS HEAT 82% AFUE		GAS HEAT 92% AFUE		GAS HEAT 96% AFUE	
	CCF/YR ¹	COST/YR ²	CCF/YR ¹	COST/YR ²	CCF/YR ¹	COST/YR ²
Example 1	787	\$453	682	\$408	604	\$362
Example 2	940	\$554	848	\$500	712	\$479
Example 3	1098	\$647	989	\$584	848	\$550

¹ Gas used per year measured in hundreds of cubic feet (CCF) at

² Gas cost based on \$6.00/CCF

Save \$50 to \$200
When You Buy Now!

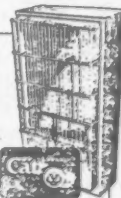
At these sale prices, you're getting a good deal. But it's an even better deal if you're a qualified Minnegasco customer.

- 12% s.p.r. financing, 48 months to pay (minimum monthly payment required)
- Or, 90 days to pay, no interest
- Quality brand names
- Authorized Minnegasco service
- Installation available

All New Room Heating with The Cat™

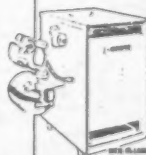
Put heat where you need it—and save money on your heating bill—with The Cat gas room heater. The Cat combines modern technology with comfort and convenience.

- vented for safety
- thermostat lets you control heat by temperature setting
- wall mounted to take up little space



Well-McLain VHE Gas Boiler

87% efficient. A long-term, long-lasting investment in home heating. Corrosion-resistant cast iron construction for long life, maximum efficiency. Top quality safety controls for years of automatic, trouble-free heating.



Energy-Saving Installed Insulation

Save now on installed attic insulation and ventilation. Call for a free estimate.

1650 Mankato Mall
387-1111

Sale ends February 17.

Minnegasco
Centers



Attachment C

MAYTAG HIGHLANDER DRY CLEANING

LAUNDRY 920 N Front 625-9776
 Maytag Highlander Self-Service Laundry
 Center Belle Mar Mall 625-9741
 Maytag Highlander Self-Service Laundry
 Center 920 N Front 625-9776
 ICBRIDGE ALZANDER N DR MD
 Medical Office Ltg 310 Belle Av. 625-5256
 Residence 1100 Lori Ln. 388-5706
 If No Answer Dial 387-6543
 McCarney Joe Ins 388-5665
 629 N Front Old Town 388-4201
 Residence 112 Garden Blvd 388-4201
 McClure-Harrington Mary Ins 345-7670
 113 Monroe Av NW 625-4256
 Residence 1024 Center NW 245-3950
 McCollum Lloyd Sawmill St Clr 388-2632
 310 Fulton
 McCough Robert/Elec 257-3083
 305 Maywood Egl Lk 625-3425
 McDonald Tim Ins 227 E Main 387-4624
 Residence 819 Range NW
 McDONALD'S INTERIOR DESIGNS 625-9013
 631 S Front
 McDONALD'S RESTAURANT
 1411 Madison Av 345-3270
 Hwy 169 N 625-7178
 McGarvey Coffee Inc. 387-3020
 McGOWAN PENNIE W CB
 Jct 169 S & 68 387-3863
 MCGOWAN WATER CONDITIONING INC
 401 Eleanor Ltrr 388-3361
 Or 388-3371
 MCGREGOR HYDRO C DR MD
 Mankato Clinic 625-1811
 Residence 100 Oakwood Dr 387-8162
 McHugo K T Office 210 Walnut 345-6474
 Residence 1004 E Main 387-2715
 McKinnis Doris C 105 Homestead Dr 387-5661
 McLaughlin David Catty 400 Graff Bldg 387-3188
 McLean Edward D ally
 Twin City Federal Bldg 387-3155
 Residence 300 S 2nd 387-7678
 McLEAN PETERSON SULLIVAN HAUGH
 & RIEDY attys
 Twin City Federal Bldg 387-3155
 113 S Main Lk Crystl 726-2138
 Vernon Center Office Vrs Cntr 345-4734
 McMullen Keith Ins 405 Martin Bldg 345-1648
 Residence 917 Baker Av 387-7862
 MCPHERSON FARMERS MUTUAL FIRE
 INS CO St Clr 245-3434
 McVicker Denny Ins 310 Graff Bldg 388-2612
 Residence 102 Daniel Ct 387-4276
 Meadow Mary Jo PhD psychlgst
 1204 Highland Av 387-4276
 Meadow View Apartments
 1261 Pohl Rd 345-6951
 Medco Corporation 110 Hickory 388-9307
 Medical Marketing
 101 E Main Lk Crystl 726-2612
 Medicare Information-Social Security
 Administration 101 N 2nd 387-7923
 MEDICINE SHOPPE
 340 Belgrade Av NW 387-6521
 Medo Evangelical Lutheran Church
 RFD 2 Mtn 869-3056
 MEISTER CONSTRUCTION
 RFD 3 Mtn 625-4084
 Melhorn Curtis adjtrs 1027 N Front 387-1141
 Residence 2224 Clare Dr NW 388-1319
 MELHORN-MUELLER CO
 1027 N Front 387-1141
 Mel's Buick & Implement Co. Amby 674-3457
 MEMORY MAJOR COUNTRY STORE
 Mdn Lk 243-3237
 Menne Scott Jr est 518 Pike 345-8554
 Residence 120 Mary Lou Ln 625-5446
 Mennonite Church Mankato
 1735 E Main 387-1373
 Mercantile Motor Co 1620 N Front 625-1578
 MCKEITH DORAL C MD
 Orthopaedic & Fracture Clinic PA
 Telephone Answered Day & Night
 309 Holly Ln 388-6889
 Residence 40 Hamlen Dr 345-3563
 Merrick Donah N Dr 801st 730 Madison Av 625-2021
 Residence Elysian 243-3462
 Mer's Hair-Em 108 Dane 387-6801
 Merle Norman Studio
 2090 Mankato Mall 387-7104

MERTSDORF DUANE Ins

100F Bldg 129 E Jackson 387-5641
 Residence Vrs Cntr 549-3551
 Mesaba Airlines
 Mankato Municipal Airport 625-2511
 Messiah Lutheran Church-ALC
 1706 Lee Blvd NW 387-5537
 METAL PRODUCTS MANUFACTURING
 RFD 7 Mtn 947-3718
 Methodist Belgrade United Church
 325 Sherman NW 625-3759
 Methodist Church Centenary United
 2nd & Cherry 387-4073

METRO SALES INC

79 Navaho Av 345-8041

Metropolitan Life Insurance Company
 Mankato District Sales Office
 Suite 310 Northwestern Office Bldg
 209 S 2nd 625-1675
 Metropolitan Property & Liability Insurance
 Company
 Suite 310 Northwestern Office Bldg 209 S
 2nd 625-1675
 Mettler's Bar & Restaurant
 117 S Front 625-9660
 Mexican Village Restaurant
 1630 Madison Av 387-4455
 Meyer Daniel H atty 115 E Hickory 345-1179
 Residence 1022 Shady Oak Dr NW 387-6902
 Meyer Philip Ins 227 E Main 625-9400
 Residence 217 Maple Ridge Dr Mtn. 278-3100
 MEYER RICHARD H DR MD
 Mankato Clinic 625-1811
 Residence 100 Heather Ln 625-7080
 Meyer Ronald H Ins
 Northwestern Office Bldg 345-7993
 Residence 5350 N 4th 387-3949
 Meyer Snowplow 502 Harper 387-7316
 Meyer & Sons Inc 227 N Front 345-4688
 For Emergencies After Business Hours
 Call 388-4402
 Or 345-3614
 Meyerling Center Harry
 109 Homestead Dr 387-8281
 Meyers Charles Jr est
 Midwest Plaza Bldg 505 Long 345-1121
 Residence 321 Kingsway Dr NW 388-1382
 Meyers Raymond Campground
 RFD 1 Mdn Lk (Long Distance) 1267-4524
 Michaelitz Agency Inc 112 Marshall 387-4081
 Michaelitz Agency Inc 112 Marshall 625-5876
 Michaelitz William J Dr MD 501 Holly Ln 625-1811
 Residence 1828 Marie Ln NW 625-1589
 Michel's Canoe Livery RFD 1 Mtn 625-6749
 MICHELS DATSUN/NISSAN
 619 N Front 387-5583
 MID INC 1911 Lee Blvd NW 625-6426
 Micro Learningware
 PO Box 307 Hwy 66 S 625-2205
 Mid-America Antenna Systems
 511 Franklin 388-8316
 Mid-America Pipeline Company
 Vrs Cntr 549-3838
 Mid America Satellite TV 115 S Broad 345-1247
 MID-BELL MUSIC CO INC 822 S Front 625-8231
 Mid-Central Realty
 Peoples State Bank Bldg Mdn Lk 243-3639
 Mid-Central Veterinary Supplies Inc
 155 Chestnut 345-7892
 Mid-Communications Inc
 221 E Hickory 387-1151
 Application For Service
 Moving Of Telephones-Bills
 Directory Listings-Etc
 Business Office 387-1151
 General Office 387-1151
 Assistance In Calling 0
 Time Of Day 345-5611
 Directory Assistance 411
 Repair Service 611
 Location Of Buried Cable 611
 MID-STATE MECHANICAL SERVICES INC
 1706 Camd Ln NW 388-1572
 MIDAS HUFFLER SHOPS
 1050 Madison Av 345-8206
 Midcom Unit - See Midland-Ross Corp 14000 Div
 MIDLAND-ROSS CORP MIDTEX DIV
 1650 Tower Blvd NW 625-6521
 MIDTEX DIV-MIDLAND-ROSS CORP
 1650 Tower Blvd NW 625-6521

MAY-MIN 17

Midhun Douglas L LPA EA
 Ofc 114 S Main Lk Crystl 726-6761
 Residence 122 N Lakeside Lk Crystl 726-6110
 MIDWAY UNIFORMS
 426 Victory Dr Bellemar Mall 387-6243
 MIDWEST ACCOUNTS SERVICE INC
 108 Hickory 388-6208
 MIDWEST AGRI-CUILDERS
 RFD 6 Mtn 625-6549
 Midwest Agtax & Marketing
 324 1/2 S 2nd 345-1085
 Midwest Business
 Machines Inc - See Rolithe Corporation
 Midwest Cash Register Co 345-1922
 MIDWEST ELECTRIC PRODUCTS INC
 Hwy 22 N 625-4414
 MIDWEST EUNTY CORP
 Midwest Plaza Bldg 505 Long 387-1121
 Midwest Filter Service RFD 1 Mtn 625-1697
 Midwest Finance Co 203 Terrace Dr 625-3934
 MIDWEST FOOD DISTRIBUTORS
 304 N 2nd Old Town 625-9301
 Or 625-3744

MIDWEST REALTY
& MORTGAGE CO

Residential Dept
 Midwest Plaza Bldg 505 Long 345-1121
 Commercial Dept
 Midwest Plaza Bldg 505 Long 387-1121

MIDWEST REFRIGERATION

Mankato 388-3055
 Midwest Shares Inc
 Midwest Plaza Bldg 505 Long 387-1121
 Midwest Vision Centers
 1517 Mankato Mall 387-4227
 Milliana Mutual Insurance Co
 139 E William Albert Lea (Long
 Distance) 1373-1130
 MILK HOUSE 722 N Front 388-4428
 Miller Bruce G atty
 Suite 200 Northwestern Office Bldg
 209 S 2nd 387-6654
 St Clair Ofc St Clr 245-3785
 Residence St Clr 245-3905
 Miller Drainage RFD 1 Lk Crystl 726-6737
 Miller Greg P DDS
 1720 Lor Ray Dr NW 345-5464
 Residence 1105 N 6th 345-8511
 MILLER MEDICAL SERVICE
 2144 Hoffman Rd 625-1054
 MILLER MOTORS TIME CENTER
 518 S Front 345-4671
 Miller Randall Insurance Agency
 405 Graff Bldg 387-6786
 Residence 116 E Glencrest Dr 387-1365
 Mini Storage-Deke Ben Transfer
 417 Poplar 345-4617
 MINN CATV INC
 228 S Front 388-9311
 Minn Kota Inc 1531 Madison Av 345-4623
 Minneapolis Star and Tribune
 413 Patterson Av 345-3216
 MINNEGASCO
 1650 Mankato Mall 387-1111
 EMERGENCY SERVICE (Answered 24
 Hrs) 345-4605
 If No Answer Call Collect 625-4605
 Appliance Sales (Answered 24 Hrs) 345-4605
 Buried Pipe Locations 345-4605
 Minnegasco Center
 Account & Credit Information/Business
 Office 387-1111
 Appliance Sales 387-1111
 Region Headquarters 2400 N Front 625-5611
 Minnesota Cemetery Ass'n RFD 9 Mtn 625-8707
 Minnesota Concrete Products Co
 RFD 9 Mtn 625-5369
 Patrick Collins St Peter 931-2978
 MINNEAPOLIS GOLF CLUB RFD 9 Mtn 625-5777
 Minnesota Sawmill RFD 9 Mtn 625-5575
 MINNESOTA ADDITIONS CENTER
 350 Martin Bldg 345-4679
 MINNESOTA AUTOMOTIVE INC
 1911 Lee Blvd NW 625-6486
 Hanger Mankato Airport 625-3993
 MINNEAPOLIS BUILDING CENTER INC
 RFD 2 Box 48 Mtn 626-3867

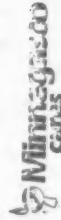
BUSINESS LISTINGS

Conditions and limitations of your Service Plus Contract. Please read carefully and save.

- 1 This plan applies to one single family residence per zip code.
- 2 Equipment must follow code requirements and be in operating condition to be covered by Service Plus.
- 3 Minnegasco shall not be responsible for charges for service or parts you have others provide.
- 4 Minnegasco reserves the right to restrict specific makes of equipment, and the availability of parts, and the choice of parts to be used as at the discretion of the repairman.
- 5 If Minnegasco estimates the cost of repair to be more than the value of the appliance, Minnegasco reserves the right not to repair the appliance and to recommend replacement by you.
- 6 Minnegasco will not be responsible for direct damages, consequential damages (indirect losses or injuries), losses or injuries caused by delays, failure to perform, unavailability of parts, loss of services, and other conditions beyond control of Minnegasco. Minnegasco shall not be responsible for any damages or losses to all or any part of its obligation under the terms of this plan.
- 7 This plan does not cover any material, parts and labor required as the result of abuse, vandalism, fire, freezing, acts of God, power or water supply outages, flooded cells or other abnormal conditions.
- 8 Minnegasco will automatically renew the plan at the end of 12 months, to assure continued protection. You may cancel the plan at that time by notifying Minnegasco by mail.
- 9 You are purchasing the plan for one full year. The price quoted is a one-time fee. If you cancel the plan within the first 30 days, you may transfer the plan to a new incident if you move.

Here is what Service Plus does not cover:

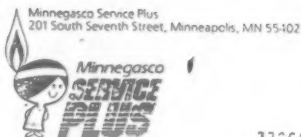
- 1 Labor and materials for repair or replacement of these parts: Tumblers, light bulbs, panels (including glass), insulation, heat exchangers, water tanks, chimneys, chimneys, Class 8 chimneys, water heaters, air cleaners, boiler actions, expansion tanks, feed water pumps, pressure pumps, pressure pumps, pressure pumps, pumps, boiler motors, panel systems, and floods independent of an oven.
- 2 Labor and materials for cleaning of boiler water, draining of expansion tank, venting of radiators, setting of air flow to rooms, cleaning of air ducts, cleaning of cooling coils. Disconnection of appliances for cleaning, installation of appliances.
- 3 Any other labor and parts not shown on the Coverage Chart.



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BULK RATE
U.S. Postage
PAID
Permit No. 343
New Brunswick, NJ

APPENDIX E

SUMMARY CASE REPORTS OF
UTILITY COMPETITION

Alabama

A Contractor questioned whether Alabama Gas Company was subsidizing gas grills. In a complaint filed with the Alabama Public Service Commission, the Commission denied his request without even so much as a hearing.

Florida

Contractors have protested to the Governor's Energy office on Florida Power & Light's plan to supply water heater insulation kits which it would obtain directly from the manufacturer and sell and install for "roughly half of a contractor's installed price."

Peoples Gas System offers cash allowances to customers for converting from electricity or oil to natural gas and to builders installing gas equipment in new homes. (Note that promotional allowances were one of the key issues studied during the 1968 Dingell hearings.)

Idaho

Contraction associations filed a complaint with the Idaho Public Utility Commission. As a result, Intermountain Gas Company discontinued operations of "Homeguard Systems."

Idaho, Montana, Oregon, Washington

Bonneville Power Administration is reviewing a plan which proposes incentives to encourage high efficiency appliances and incentives for the removal of older appliances. The Regional Conservation and Electric Power Plan was developed by the congressionally created Northwest Power Planning Council.

Indiana

Natural Gas and Coke Utility of Indianapolis recently implemented a program to provide service on air conditioning and heating units for residential consumers. However, contractors met with the utility to explain their objections and the utility had agreed to phase out the service program.

Boonville Natural Gas Company of Boonville promotes servicing work right on the gas bill. They offer "Air Condition start-up special & clean & oil unit & check major components. Start May 12, 1983, \$34.95."

Massachusetts

Bay State Gas advertises that it rents the Energy Stretcher water heater for \$8.50 a month which includes free installation and maintenance.

Missouri

Laclede Gas Company of St. Louis has entered into the service, repair, and installation of gas appliances for residential and commercial consumers. Utility programs include gas water heaters, space heaters, and gas bar-b-que pits, as well as insulation, insurance and security protection systems. Laclede offers one day loan approval at a rate 2% less than Mastercharge. Advertising is sent with the gas bill and billing is done on the gas bill.

Area contractors note that while the average growth of successful service companies has been less than 40% in the last 5 years, the utility has almost doubled their service work and service personnel.

The Plumbing Contractors Association of Metropolitan St. Louis, Sheet Metal Contractors Association, and the Air Conditioning - Refrigeration Contractors Association have filed an intervention in the utility's rate increase request charging that the service work is being cross-subsidized by the rate payers.

New Hampshire

Keene Gas Corporation advertises a 30 gallon water heater for \$149 (with free gas and plumbing installation) even less than a supplier can get the product for, let alone sell it to a contractor.

New Jersey

A contractor there has protested to the New Jersey Board of Public Utility Commissions over Elizabethtown Gas advertising, credit and collection procedures which place contractors at a competitive disadvantage.

New York

After a major battle before the Public Service Commission, the Long Island Light Company was denied authority (without prejudice to future reconsideration) to create a wholly owned subsidiary. An internal LILCO document "recommends that we (LILCO) refrain from doing business with Burns .." since Burns Heating & Cooling was a leader in the complaint against LILCO.

Nevada

Sierra Pacific Power Company, Reno, Ne., is featuring the White-Rodgers Comfort-Set clock thermostat in promotional mailings to its 170,000 gas and electric customers. The company invites customers to purchase items from its mail-order catalog of energy-saving products. Different products are featured from time to time on its monthly billing envelope.

North Carolina

Supported by his state PHC association, a North Carolina contractor filed a complaint before the North Carolina Utilities Commission alleging that Piedmont Natural Gas Company was selling and renting water heaters at below cost. The Commission has agreed that the complaint should be heard. However, the contractors have spent more than \$9,000 thus far and they have had to hold back on pursuing the complaint because of lack of funds.

Ohio

East Ohio Gas Company offered free water heaters for a while to encourage consumers to hook up to the gas lines.

Cincinnati Gas & Electric (CG & E) of Cincinnati is installing free "curb boxes" and checks for gas leaks at the same time. When they find a leak, they offer to repair it for \$75.00. Alternatively, they suggest to the consumer that he can call his plumber, but the plumber will have to pay CG & E \$75.00 for permits in addition to charging for time and materials.

Oklahoma

Public Service Company of Oklahoma has been sued by 4 outdoor lighting companies for monopolizing business in the area by furnishing services below cost. The 4 companies charged that the utility has abused its public utility status by installing and maintaining outdoor lighting on private property while refusing or stalling on their requests for hookups for their own lighting installations.

The utility denied it supplied its services below cost. It also argued that as a state-regulated entity it was exempt from federal antitrust statutes.

A federal district court upheld the utility on the grounds that there was no evidence that interstate commerce had been adversely affected. However, the U.S. Court of Appeals said the companies only had to show that interstate commerce was affected. The appellate court has ordered a retrial of the antitrust suit.

Pennsylvania

Contractors have been opposing Peoples Natural Gas attempt to use their unneeded excess capacity of service people to provide service contracts.

Tennessee/Virginia

Following protests from contractors to the Tennessee Public Service Commission, the Tennessee-Virginia Energy Corporation did abolish the EADS Sheet Metal and Air Conditioning Company that it had bought.

Vermont

Central Vermont Public Service Commission advertises water heater jackets obtained through its "special purchase buying power" and offers them at "a selling price under our actual cost" (emphasis provided by the utility). In a telephone conversation with the staff of the Vermont Public Service Board, they reported that this cross-subsidization simply was not an issue in the last rate case.

Mr. LUKEN. Mr. Hager, these petitions that you have just outlined at the conclusion of your statement—have you addressed them to the State?

Mr. HAGER. About 2½ years ago, we addressed something similar to the public service commission. I appeared before them. And they did force the gas company—

Mr. LUKEN. All right. How about to the State legislature or the Governor?

Mr. HAGER. No, sir.

Mr. LUKEN. Could we discuss that for a minute?

Just what are the possible solutions, assuming that—we are impressed with your very cogent presentations and the fact that you are being discriminated against—that the regulated monopoly is subsidizing competition against you, and that would seem to be unfair by just standards of fair play; there ought to be a law against it.

We are searching around as to what laws there are and what laws we might consider. Do you want to enlighten us a little bit about just what investigations you have made about that?

Mr. LAVALLEE. I am simply going to comment on the State law side of things. I think as this has become a growing matter of concern on the State level, there have been some States that have started to address this legislatively.

California has passed one bill which does prohibit the utility involvement, although it is one that admittedly is without teeth at this point. There is a second bill which is being pursued through the California legislature now, which, as I understand it, will put greater teeth in the prohibitions against utility involvement in California.

In Pennsylvania, there was concern 2 or 3 years ago regarding the service lines which go to the house, which at least in one part of Pennsylvania—in the Pittsburgh area—was the province of contractors. There had been some interest on the part of the public service commission of making that the province of the utilities.

The contractors and other small businesses expressed a great deal of concern. Legislation recently was passed which prohibits the utilities from doing the gas service lines. Those now remain the province of contractors.

There is a second bill which has been introduced into the Pennsylvania legislature and they have had hearings on it, which would prohibit other utilities from supply and installation activities.

There are other States that have expressed interest in similar legislation, and I think we are beginning to see a greater interest on the part of States to address this through State legislation, and I think—as some of us have said in our statements, I think we would agree that some of that should be at the State level.

Part of the reason why I think we are here today is that some of it has been brought to the Federal level, either by way of Federal legislation, such as the legislation on RCS and CACS, or by way of weaknesses in the antitrust laws or that the utility commissions don't have the ability or the desire to focus on competition issues.

I think these are a number of factors that suggest some Federal attention.

Mr. LUKEN. Offhand, it seems to me that the utility commissions have a point—that they were not constituted to deal with competition of this nature. Wouldn't you agree?

Mr. LAVALLEE. And that is fine if that is the conclusion of the public service commissions in the States, but if that is the case, some other mechanism or relief is necessary.

It appears that one of those other mechanisms may be either the antitrust laws or assistance from the Federal Trade Commission. It may be that another form of relief is seeking State legislation to actually cover those sorts of situations.

Mr. LUKEN. Up to now, only California has passed a State law, and that one without any sanctions.

Mr. LAVALLEE. That is the first one that I am aware of; that's right.

Mr. WEBER. Would the chairman yield?

Mr. LUKEN. I would be glad to yield.

Mr. WEBER. I just wonder, along that line—this seems like a new problem, and yet I don't detect a reason why it would be a new problem.

How come we haven't faced this problem before? How come we are only now seeing a real problem created here that needs to be addressed at the Federal level?

Mr. LAVALLEE. I think it is a recurring problem—if I may—and that is that we did have some competition between the utilities, gas and electric, which produced the 1968 congressional hearings, and in fact, admittedly, we have had the comparison presented to us by the gas industry that they see this much like a David and Goliath—that they are the David attempting to slay the Goliath—and that therefore they need to provide many of these promotional practices to ensure that gas appliances and gas equipment are used, and they would argue that the electrical industry has even far greater resources.

We are the small businesses; we are the ants on the field being stomped upon while the gas and electric utilities fight it out.

It has been addressed in the past, and in the past the competition tended to be more in the area of energy consumption. In the late 1970's, there was a switch more toward energy conservation, and as utilities were attempting to promote energy conservation, they were at the same time trying to at least maintain, if not increase, their market share.

So you try to make your particular equipment or appliances look more efficient while trying to sell more of your appliances or equipment, so that you essentially tie in the sale of your particular type of fuel type.

Mr. WEBER. I thank the chairman for yielding.

Mr. LUKEN. I am interested in the installer question. You run into competition there, and that's sort of a backdoor entre for the utility company to get into the appliance business or whatever product they are selling. Is that right?

Mr. JOHNSON. That is correct.

Mr. LUKEN. Would you want to expand on that at all?

Mr. JOHNSON. You might repeat—

Mr. LUKEN. Pardon?

Mr. JOHNSON. If I understand you correctly—

Mr. LUKEN. Well, you mentioned the installer—that the utility selects from a bank of installers. They make up the list, and they select the installer——

Mr. JOHNSON. That's correct, in our area.

Mr. LUKEN [continuing]. Of the appliance or of the furnace or whatever it is. And obviously the installers then are in competition with each other. The installers are often associated with a company; they don't just do installing; they also sell the product, don't they?

Mr. JOHNSON. That's correct.

Mr. LUKEN. So their competition just might discriminate against the installer who is associated with a company that is in competition with the gas company—would be normal business behavior, shall we say.

Mr. JOHNSON. The installers in our area, even though they may choose to install for the gas company, are not supportive of the program at all.

Mr. LUKEN. They are not supportive of what program?

Mr. JOHNSON. Of the gas company retailing appliances and water heaters.

Mr. LUKEN. Are these installers independent installers?

Mr. JOHNSON. They are independent.

Mr. LUKEN. They are all independent?

Mr. JOHNSON. Yes; they are paid an installation fee.

Mr. LUKEN. That's why I asked the question. I thought some of them would be. But they also work not only for the gas company, but they work for the retail sales organizations.

Mr. JOHNSON. They often are a retail sales, themselves.

Mr. LUKEN. Let's get back to that again. The installers are also in retail sales.

Mr. JOHNSON. Well, are we talking about the mechanic, or are we talking about the company?

Mr. LUKEN. I don't know. You mentioned installers. I want to get into that.

Mr. JOHNSON. OK. In our area—and I am sure there are some examples that may not fit this, but the installing contractor has a mechanic that he will send out on a job to install materials which he has sold.

Mr. LUKEN. And the installing contractor may be, at one and the same time, a retail sales——

Mr. JOHNSON. That's correct.

Mr. LUKEN. The installing contractor is an integral part of a sales organization.

Mr. JOHNSON. The existing one that is in place today.

Mr. LUKEN. Right. So they don't exist independently, but those installers, therefore, are on the list that the utility company selected.

Mr. JOHNSON. That's right.

Mr. LUKEN. And obviously the temptation would be there for the utility company not to select the installer who happens to be a strong competitor for the utility company in the sales field.

Mr. JOHNSON. You are very perceptive. I hadn't thought. Yes; surely.

Mr. LUKEN. I think Mr. Weber makes the sage observation that it seems strange that so many of these things seem to be new, when it would seem that the problems would have been around and you would have noticed this—you would have had this experience.

Mr. HAGER. Mr. Chairman, may I speak?

Mr. LUKEN. Yes.

Mr. HAGER. Generally in our community, the gas company—what they will do, they will choose a young licensed contractor that is just starting out, that doesn't have very much work. They will not generally choose a company that is established and in direct competition with them.

Mr. LUKEN. So you have had that experience?

Mr. HAGER. That's correct; because I refused to install their equipment because I'm losing the profit on it, and paying a union wage, I just can't compete and stay in business just selling labor; I've got to sell a product.

But there's always some young, new company that starts up that utility companies hire to do their work, because they have nothing else, you know; they haven't got a reputation built up.

Mr. LUKEN. What has been your experience with reference to appeals to the utility commission?

Mr. HAGER. Well, before I was saying that they did—2 years ago, they did make Minnegasco restructure their whole financing of their servicing. So they came out with a policy with big half-page ads in our local paper: "The public utilities commission ruled that we can no longer service your water heaters," and so forth, free. "We will have to charge between \$50 and \$60 an hour for your service. But we have a savior. Join our Maxi-Plan for \$5.95 per month. You will not have to pay the \$60-per-hour of overtime pay for service calls in the dead of winter." And they made it real, a half-page ad in the paper.

Mr. WEBER. Would the chairman yield, please?

Mr. LUKEN. Yes, I'll be glad to yield.

Mr. WEBER. Can you tell us what kind of effect—I'd like later to get into this question more broadly, but can you tell us specifically what kind of an effect that policy has had on your sales?

Mr. HAGER. I would say other contractors and I are probably affected 60 to 80 percent.

Mr. WEBER. That's on what items?

Mr. HAGER. In sales of heating equipment, and probably more so—

Mr. WEBER. What percent of your business is heating equipment?

Mr. HAGER. I would say probably 25 percent.

In the actual servicing of equipment, it would probably be affected more so.

Normally during a Minnesota winter when it is 25 below zero, we would have 25 heating calls on a given day. This past winter, we had like two or three; it's unbelievable.

Mr. LUKEN. I'd like to address this to the association representatives.

Is this a situation which is uneven around the country, a situation where we don't have any commonality within the various congressional districts, within the various cities and the various

States, so that you as representatives of your associations might even have a little bit of difficulty in organizing the constituency that you know is out there?

Mr. LAVALLEE. You are very true there. It is widely divergent. We do have some utilities where there are some very cooperative relationships between the contractor groups and the utilities, and then there are other areas where there are some very severe problems.

We have done some surveys with associations in our coalition to try to identify the States. Minnesota was one that several utilities that sell gas were identified. Particularly, since it was the members of the plumbing, and heating, and cooling contractors, their responses are going to be a little bit more geared toward gas. Involved in our coalition are also some of the electrical contractor groups, and they are having as much problem with some of the electric utilities.

But it does tend to be on an area-by-area sort of a thing, and I can recall that there have been some situations in individual States over the years where small businesses have attempted to fight it, but they saw it as primarily a State or local issue.

I think it has only been in the very recent years that there has been renewed attention or focus on the fact that, yes, this does have some national proportions. Because, it does cross into the Federal threshold in some areas. In other areas, it's simply an exchange of information so that States can develop strategies to combat the problem in other States. If you know what is going on in one place, then——

Mr. LUKEN. How long has your organization been in existence?

Mr. HAGAR. A hundred years. We are the oldest in the construction industry trade association.

Mr. LUKEN. You weren't organized then, obviously, particularly for this?

Mr. HAGAR. No. It has been to promote the health and sanitation of the potable water supply, because we originally started out as a plumbers' group. As many plumbers became more involved in the broader range of things, including heating and cooling, we expanded our membership base to include those sorts of things, at least for the plumbing, heating, and cooling contractors.

Mr. LUKEN. How long have you been in this issue?

Mr. GREENE. Well, Mr. Chairman, I kind of got involved in this issue on my own without any association or anything.

Basically, back—you mentioned the public service commission. I was concerned about the diversification of the utilities on my own, basically, just as a small businessman here in the area, without really approaching my association beforehand.

I, upon myself, received or happened to read an article in the newspaper that our local utility was asking for a rate increase, and they were going to be holding hearings in front of the public service commission.

I felt that a very good opportunity to get into the front door and express my concerns to the public service commission, and express our concerns as far as diversification and why are they asking for more money for utility rates when here they have all this money they seem to be diversifying with.

Back in January of 1982, I addressed my concerns to the Maryland Public Service Commission in Baltimore, and they responded within a week's time with a letter stating that they did receive my concerns and they would investigate the situation and get back to me.

It took a little over a year, and I finally received a response from the Public Service Commission of the State of Maryland, and it was basically a page and a half, and all it really said, in four or five paragraphs was that they looked into the situation of cross-subsidization and diversification, and so forth, and they don't see anything that is affecting my gas bill, and, "Thank you very much for your inquiry," and so forth. And that was the extent of the type of service that I got from the Maryland State Public Service Commission.

Since that time, I have joined forces with our association, because I did learn that it was something that was ongoing throughout the various areas of the country, and that's basically when I have really gotten involved with it.

But I go back with documentation back to January of 1982.

Mr. LAVALLEE. Can I provide another analogy, if I may?

Mr. LUKEN. Yes.

Mr. LAVALLEE. I think that it is similar to not knowing that something may be wrong until someone tells you. You take things for granted.

I think we did have a situation in our industry in recent years in which—and I'm not claiming that our members are ignorant; that's not my intent at all, but that we have situations where someone suddenly realizes, "Oh, you mean it's illegal to have my pocket picked at 9 o'clock every night?" They didn't realize that.

I can tell you the story of one contractor's reaction while we were talking about a free water heater program in one State. We were talking about it and saying, you know, how unfair that was that they were providing water heaters. And he said:

Oh, boy. At least that problem's not as bad as mine. They have taken over the ten-year guaranteed water heater market, but I'm able to compete with them for the five-year water heater market.

And then he kind of paused, and he caught himself, and he suddenly realized that they had taken over one part of the market, and the only way he could compete was by offering a lower priced item, and he realized suddenly that the problem was affecting him.

He thought he didn't have a problem, and then as he started to think about it, it suddenly started to click. And I think that has been the case, that we have explained to our memberships some of the problems around the country. Fortunately we have some members who were working on it and identified it, but we had many others who didn't realize that their business was being adversely affected.

They were little fellows. They don't have that macro look to be able to see what is affecting their industry across the board, and until they start seeing some of those effects that have occurred in other areas and suddenly realizing, "Hey, wait a minute; that's the same thing that is happening here."

Mr. O'CONNOR. We in the American Supply Association had a member in Baltimore who, for many years, was selling a small

valve—a hot water heater valve—to our gas and electric utility in Baltimore, and he never really thought of the consequences of utility competition until last year, as this issue started percolating within our association, and it finally dawned on him that if he was selling 7,200 hot water release valves to the gas utility every year, who was selling the hot water heater that went with that valve?

On a little investigation, he determined that the utility was purchasing directly from the manufacturer, and he then realized that, although he was getting some business from the utility, the big ticket item was being taken out of his hands. That's a problem we've seen.

Mr. LUKEN. The utility was selling the hot water heater?

Mr. O'CONNOR. The utility was selling the hot water heater. The ASA member was supplying a small valve for the hot water heater.

Mr. LUKEN. Where was this?

Mr. O'CONNOR. This was in Baltimore.

Mr. LUKEN. A Baltimore utility sells—

Mr. O'CONNOR. Sells hot water heaters.

Mr. LUKEN. Hot water heaters.

Mr. O'CONNOR. Indiana Gas is the same way. The picture you have in front of you there—you can see the hot water heater they sit in their front window.

Mr. WEBER. It's true of Minnegasco, too, isn't it?

Mr. LAVALLEE. That's correct.

Mr. HAGER. Mr. Chairman, something that's interesting is—

Mr. LUKEN. I'm just not familiar with that. In our section of the country, that doesn't happen, and that's part of the problem, obviously. We are coming from different places here.

Mr. O'CONNOR. Mr. Luken, if I might, for the record, we received last week from our supplier in Massachusetts a copy of a newspaper advertisement from Eastern Edison Co., in Fall River, MA,

Why should a nice furnace like yours run all summer long? Give it a summer vacation and save on fuel by heating water electrically. Rent an 80-gallon electric water heater from Eastern Edison for just \$5 a month. You will be heating water at the economical off-peak electric rate. No deposit is necessary, and you will receive a generous installation allowance. Plus, when you rent our conservation model electric water heater, should it ever fail, we will repair it or replace it at no charge. You'll never pay for parts or labor. And that's not all.

Mr. LUKEN. Well, let me conclude, since I've taken so much time, by asking you this question. Assuming that we would want to ban utilities from these activities, I'd like to ask each of you who would like to answer, what would you recommend? You may not have an answer, but if you do, what answer would you have to us as to what course we could follow here as the Congress of the United States?

Mr. LAVALLEE. Well, I think we all appreciate the efforts of the Small Business Administration's Office of Advocacy's contribution to this in that they initially have recommended that utilities be prohibited from the supply, installation, and service. But I think they have recognized in their report the realities that there may still be a desire in some communities that utilities may wish to do so, or that State public service commissions or other entities may want to at least entertain the idea.

What I think the Chief Counsel has done in his report is suggest some criteria that ought to be looked at and that ought to be used which are primarily the effects on competition.

I don't have the report directly in front of me, but I do recall, because I have quoted it many a time. It is on page 9, where there are several criteria listed as to whether there is substantial public benefit, whether there are existing entities currently providing service, whether protections can be built in to protect against cross-subsidies—several criteria like that.

Mr. LUKEN. Are you talking about legislation?

Mr. LAVALLEE. Well, those factors were things for the Residential Conservation Service and the Commercial and Apartment Conservation Service. For those types of programs, we have attempted to propose to the committee that they incorporate those sorts of protections.

Mr. LUKEN. Just concluding—anything further that you would recommend?

Mr. LAVALLEE. We have also addressed it some in some discussions under the Public Utility Holding Company Act, to get some protections. Another area is that we recognize correction is needed in the legislation right now on the mandate to do energy audits.

However, there are small businesses that perform those, and we believe that those should be taken out of the hands of the utilities, that those ought to be made available for the free enterprise small business community to go after and use, and that particularly it ought not to be allowed as a—

Mr. LUKEN. Well, that may be instructive if we do it, but, as we were discussing earlier, that may not, since there are a small percentage of these repairers, of these installations, that are supplying these appliances and whatever, that are actually governed by that program or involved in that program.

Now, it may be instructive, and I appreciate your making a concrete suggestion, but I'm saying that that may not take care of the whole problem.

Mr. LAVALLEE. The final area I'd like to just touch on briefly is that it's not clear to us whether the antitrust laws effectively cover this area or not. We know that the antitrust laws go to predatory pricing. It is not clear to what extent they do cover the marketing practices.

Mr. LUKEN. What conclusion would you come to after listening to the discussion from the Federal Trade Commission representative here today?

Mr. LAVALLEE. That the antitrust laws are not strong enough.

Mr. LUKEN. I would say that's a fair conclusion from that testimony.

Yes, sir?

Mr. O'CONNOR. There are several Federal laws that already address utility business practices. We have the CACS and RCS legislation; there is PURPA, which I believe is the Public Utility Regulatory Practices Act; the Public Utility Holding Company legislation, or that statute.

So the Congress is on record several times as legislating activities of public utilities, even though public utilities may be intra-state in nature in some cases. So I think clearly the Congress has the au-

thority to step in if they want to. As far as what form that law would take, I don't know at this time; I can't make a specific recommendation.

I think one of the most beneficial things that can happen in the next year is for the Congress to watch very carefully the FTC investigation and study of the utility industry, and for the Congress to be prepared to step in at any point in the course of that FTC investigation, if that is necessary.

Mr. LUKEN. Is there anything else anybody else wants to add on that question?

Mr. Weber may have similar questions.

All right. I thank you.

The gentleman from Minnesota.

Mr. WEBER. Well, Mr. Chairman, you have covered just about everything on my agenda.

I would just be interested in knowing, from Mr. Hager, do you anticipate new forms of competition from the utilities?

Mr. HAGER. In speaking to some contractors last Friday from the Twin City area, Minnegasco is already bidding new rooftop units on new construction. Now, that hasn't happened in my area, but in the Twin City area.

Mr. WEBER. What has not happened? New construction?

Mr. HAGER. New construction on new commercial buildings. Minnegasco is bidding to the owner or the contractor new furnace and air conditioning. Now, that hasn't happened in the Mankato area, but—

Mr. WEBER. You mean up to now all they have done is replacement?

Mr. HAGER. That's right.

Mr. WEBER. And you've had all the sales—or people in your position have had all the sales for new dwellings?

Mr. HAGER. That's correct; yes.

Mr. GREENE. Mr. Weber, you can see from my testimony, and it was brought out, that the utility here started on the premise of energy conservation with insulation, and they have grown from that to replacement windows and doors right to roofing, which is in direct competition with me, and just recently, kitchen remodeling.

If you can explain to me what that has to do with energy conservation, you know, this is their premise though.

So I think that they can just go right into room additions to building houses perhaps, if they wanted to, and it's just a constant expanding problem.

Mr. WEBER. Does anybody else have an answer to that?

Mr. JOHNSON. We have every reason to expect that we will see an increase also.

Mr. WEBER. In the same areas?

Mr. JOHNSON. It began from nothing and continues to grow.

Mr. WEBER. It strikes me that without knowing a whole lot about your businesses—that if they are not involved in new construction and they move into new construction, that's a fairly significant change in policy, isn't it?

Mr. HAGER. I'm sure that's the trend—at least in the Twin City area it seems to be the trend—is to move into new construction.

Another interesting thing—in bidding a commercial job, normally Minnegasco charges the owner for the gas service and the gas meters, depending on if it's multiple meter installation and so forth.

The past year now, they haven't made a charge. In fact, I called the gas company the other day on a shopping mall that I was bidding, and he said, "Oh, no." He said, "How many Btu's?" and I said, "Well, at least a million Btu's are going to be used on that." "Oh, no," he said, "that's enough usage. We won't charge you for the meters or the gas service."

Now, that's a new policy. I don't know what their theory behind it is.

Another interesting factor—in St. Paul. The gas company of St. Paul is owned by Northern States Power Co., which is a very fine utility. They are not in any competitive market. They have 11 service trucks for the city of St. Paul to take care of emergency calls, and pilot light-ups, and so forth. Minnegasco, which covers Minneapolis and the suburbs—I realize it's a much bigger area, maybe a third larger, maybe again as large—has over 220 vehicles.

So that's just the difference in the communities side by side.

Mr. WEBER. And the Federal Trade Commission has really no—I'm sorry I wasn't here for their testimony—capacity to restrict any of this, in your judgment?

Mr. HAGER. It doesn't seem to.

Mr. LAVALLEE. They have indicated that they are studying it, and they may go in and participate, for example, in public service commission proceedings or things of that sort, or provide comments to them, or whatever, to try to encourage action there.

It appeared to me from the scoping out of the testimony that they suggested a rather limited antitrust role in terms of antitrust actions and whatever, and yet to us this does appear that it is a very serious effort to take over parts of the market.

Mr. Hager has already indicated that for boilers—that he doesn't have any sales in Mankato. That market area, at least as far as he is concerned, has been taken over by the utility.

Whether there are other contractors that have had a few boiler sales we can't say at this point, but that's a clear monopolization that is not necessarily due to the predatory pricing but is due to the marketing practices which the utility is conducting in that area.

Mr. WEBER. One last thing. I know you all talked about it, but I presume that probably the greatest advantage these guys have, or at least one of the main advantages, is financing. Is that not so?

Mr. HAGER. And access to the customer.

A person has their water heater leaking, and the water is leaking above the burner. The first thing they do is call the gas company because they are afraid of an explosion. That is the first thing on their mind. The gas company comes and turns the gas off, and right away, they sell a water heater.

So it's also the financing and the accessibility.

In Mankato—I don't know if I told you this before—you can buy a 40-gallon water heater—a gas water heater that's large enough for probably a two-bathroom house, maybe a two-and-a-half-bathroom house, for \$13.05 a month, and put it right on your gas bill.

The customer loves that, because they don't even have to write a separate check. They pay for it over a three-year period. I can't do that as a private businessman.

Mr. GREENE. Mr. Weber, if I can expand on that a little bit—

Mr. WEBER. Sure.

Mr. GREENE. Under the RCS program, which was mandated by Congress back to the States to formulate a program, our State, the State of Maryland, formulated the RCS program and sent out a questionnaire to all the licensed contractors in the State of Maryland asking them if they would like to be included on the master list, so that when the utilities come out to do the energy audits, the consumer would receive this master list so that they can make their choice of a contractor that they wish to choose to do these recommendations that the audit prescribes.

We did a test survey after this program was all put together by the State of Maryland, and we did call the utility out to see how they handled the audit and what they would do at that time.

They came out; they did the energy audit. We did not receive the prescribed book that we were supposed to with the contractors, but, in turn, they basically suggested that they have an installation department that can handle the basic recommendations that they made.

So rather than giving out the State book, which they did not do, they basically turned around and said, "We can handle these items for you."

It cost me \$10 to get my name put in that book, plus—the \$10 isn't anything, but I think we have 7,000 licensed contractors in the State of Maryland, and I'm sure that there were half of them that were in there, and that's a good healthy sum, and the program is just not being handled as far as the RCS program; it's not working.

That's basically from my experience.

Mr. LAVALLEE. And let me tie in two themes that are questions that have kind of been addressed here—access to the consumer and whether there are new entries that we can expect in the near future.

I think we have a great deal of concern over the Commercial and Apartment Conservation Service which Congress created in 1980 and which only now is being implemented at the State level. It is not in effect yet, but it would require the utilities to offer energy audits to multi-family dwellings and small commercials.

If a utility is into the marketing of other products—boilers and furnaces—what I can readily envision happening is that the utility now has that access to go in and do that audit and say, "Gee, we sell that; I'll be glad to put it in for you." In fact we would have the following analogy. Whereas today you might have a Joe Hager going in and talking to a small businessman in a commercial establishment and saying, "Hey, you know, I think we can save energy here," and writing up a contract, and he would then have the work. Tomorrow, after CACS is in effect, we would have the situation where the utility sends out the audit announcement. The merchant takes advantage of this audit announcement and has an audit done. The utility comes in and says, "Hey, you can save energy and we'll put it in for you." A few days later, Joe Hager

runs into him, and the merchant says, "Gee, this is great. I had the utility come out. They did this audit. They told us how I could save energy. They put it in for me." And Joe Hager is sitting there saying, "But wait a minute. That's my business. I didn't even get a shot at it."

The access to the consumer has been a problem and threatens to be a far greater problem because there are no protections in the CACS.

Mr. O'CONNOR. One other point on CACS, too, is that the information that is gathered in those audits is retained by the utility company, and there are no restrictions on the utility company using that in their merchandising and installation arm.

Mr. WEBER. I don't have any further questions, Mr. Chairman.

Mr. LUKEN. Thank you very much, gentlemen, for your responses.

Personally, I'm going to mull over this. I think I'm going to have some further questions of the FTC and perhaps the Justice Department on this issue.

It seems to me there are too many similarities to the telephone case.

When we considered the telephone legislation, and when Judge Greene considered it, and when the previous judge considered it for the consent decree, these kinds of things were not permitted either by the courts or would not have been permitted by the legislation which we considered.

So why there is that discrepancy I don't know, but I intend to think about it, just as you folks—just as the FTC said they are thinking about. We'll think about it seriously.

I'm afraid that we have another call here, and I hesitate to start someone else. All right. We will recess for ten minutes.

[A short recess was taken.]

Mr. LUKEN. Thank you for your patience. We will resume this hearing and move on to the next panel. We have scheduled Mr. Thomas Morron, vice president of Edison Electric, and Charles Zeigler, president of Public Service Corp. of North Carolina.

You are all ready. Who wants to start out?

Mr. MORRON. I defer to the CEO, Mr. Chairman.

Mr. LUKEN. All right. That's Mr. Zeigler.

TESTIMONY OF CHARLES E. ZEIGLER, CHAIRMAN OF THE BOARD AND PRESIDENT, PUBLIC SERVICE CORPORATION OF NORTH CAROLINA AND MEMBER, AMERICAN GAS ASSOCIATION

Mr. ZEIGLER. That's a very comfortable position—to have an electric man defer to a gas man. I don't know what that means.

Mr. LUKEN. You are a member of the American Gas Association—right?

Mr. ZEIGLER. Yes, sir, a member of the board—

Mr. LUKEN. All right. We have your statement, you may proceed?

Mr. ZEIGLER. Yes, sir.

I think to set the stage, if I might take just a minute to mention, the American Gas Association is composed of approximately 300

members both gas utilities and the major pipelines that deliver the gas to the utilities.

Mr. LUKEN. Before you have finished, I hope you will tell us how many of them are involved in this kind of work.

Mr. ZEIGLER. I'm not sure I can, sir, but I'll tell you what I know.

Mr. LUKEN. I won't interrupt you any more.

Mr. ZEIGLER. All right, sir.

Natural gas, of course, is used by approximately 49 million gas customers that serve approximately 160 million consumers in both residential, commercial, and industrial applications.

The gas industry supplies about 27 percent of the primary energy in the country and delivers about two and a half times the total energy of the electric industry in the form of primary energy.

My company operates in North Carolina. We serve approximately 162,000 customers. We are a small to medium size utility of the A.G.A. member utilities that were mentioned. We operate over a 10,000-square-mile area. We serve 81 communities. The largest community we serve is in Raleigh, NC, the State capital. A number of our communities are small. We serve these communities and our customers from 21 offices. We have 850 employees involved in the utility operation.

Public Service was incorporated in 1937. A form of gas has been distributed by our company in North Carolina, in Raleigh, since 1858.

A little bit of the background of the company. Our sole supplier is Trans-Continental Gas Pipeline Corp., one of the major pipelines that serves the east coast of this country.

My first comments relate to the AGA position in regard to regulated monopolies' competition with small business.

The gas industry's conservation efforts today are aimed at keeping the cost of energy at the lowest possible level in order to preserve our gas markets. The more efficiently gas is used, the lower its unit cost, the less likely fuel switching is to occur.

Encouraging energy conservation also enables our industry to flatten our demand peaks. This benefits all of our customers. Thus, conservation is in our own self-interest as well as in the interest of utility customers.

We have been in the conservation business for a long time. My company has been in the merchandising business for well over 50 years. We have been in the installation and service business for much longer than that in our predecessor companies.

Most utilities are now prohibited by NECPA from selling and installing RCS program measures. My company does not install RCS program measures. However, some pre-NECPA utility conservation marketing and installation programs were grandfathered from this prohibition.

Furthermore, a number of companies have obtained waivers from the prohibition. These were supported by each utility State Governor and were approved pursuant to the FTC's scrutiny concerning potential competitive impacts.

Opponents of utility competition have asserted that a utility is better able to compete because of its ability to cross-subsidize its marketing activities through its rate base. We believe this is a misconception.

Local utility commissions have the authority and responsibility to monitor these nonutility activities to ensure against utility cross-subsidization of nonutility activities through the rate base.

AGA believes that the hidden agenda in the efforts by some to prohibit utility involvement in nontraditional marketing efforts is the fear of competition itself.

The only logical rationale for such a prohibition is not to protect competition, thereby protecting the consumers, but the goal is to protect utility competitors. To suggest that somehow the utilities are inappropriately entrants in the market addressed by NECPA is to penalize the consumer, who would no longer be able to benefit from utility efforts.

Some have also alleged that utilities are in the position to act anticompetitively because they are guaranteed a rate of return by their State utility commissions.

Contrary to this claim, gas utilities are not guaranteed any particular rate of return. They are given an opportunity by the State regulatory commission through approved rates that are designed to afford a utility a reasonable opportunity to achieve its allowed rate of return. In fact, it is not uncommon for utilities to fall below the authorized rate of return.

In addition to marketing appliances and equipment, gas utilities compete with private businesses that specialize in providing onsite residential and/or commercial energy audits. This utility competition is mandated by NECPA.

This, coupled with the statutory mandated subsidization of the audit cost above the \$15 maximum, can give a competitive advantage to the utility in the energy audit business.

The gas industry never sought this advantage. This subsidization was mandated by Congress. In fact, AGA has consistently opposed this subsidization since NECPA was in its legislative infancy. Indeed, we strongly advocate repeal of both the RCS and CACS programs.

Alternately, we urge Congress to allow utilities to charge RCS and CACS program participants the full cost of the audits.

Through involvement in the sale of gas equipment, gas utilities promote the sale of gas even when the utility does not merchandise the equipment. Utilities that market appliances and other equipment usually do not offer the lowest prices. Generally, utilities handle medium and upper priced products.

Many nonmarketing gas utilities advertise gas appliances and equipment generically to encourage gas sales. This type of promotion has obvious benefits for heating and cooling contractors who might not be able to push the sale of gas appliances and equipment on their own.

Most utilities maintain an active liaison with local contractors. That includes educational programs to alert contractors to the latest local code requirements affecting equipment installations.

Furthermore, in other instances, gas utilities cooperate with local code officials in assuring that gas installations and services are not extended to new construction that does not comply with energy efficiency and safety provisions of local and national codes and standards.

In addition to competing with small businesses and marketing appliances and other consumer goods, utilities provide service calls to consumers whose gas appliances or equipment need repair.

In a number of instances, utilities provide true emergency services for their customers just by responding to calls concerning suspected gas leaks. Providing these safety calls plays a vital role in preventing damage that could result from undetected or unrepaired gas leaks and faulty equipment.

Although this service can be performed by nonutility businesses, in many instances the gas utility may be the only source for emergency assistance. Most utilities operate 24 hours a day and have people on call 7 days a week.

Thus, safety-related programs are a valuable service to utility customers and help to ensure a level of service that is commensurate with the interests of public safety.

There are three main reasons gas utilities seek to diversify: one, to preserve and expand gas markets; two, to secure present and future gas supplies; and, three, to improve their financial stability.

Improved financial stability and strength should lower the company's cost for capital, thereby saving money for gas consumers.

The NARUC 1982 report of the Ad Hoc Committee on Utility Diversification did not endorse utility diversification without qualification. However, it agreed that there are many legitimate reasons that can justify diversification by a utility into areas both functionally and nonfunctionally related.

During the past ten years, total investment risks for gas utilities has increased both absolutely and relative to other industries, as measured by debt ratios. Relative risk was reflected in a recent AGA study which was made in 1982.

Distribution companies exhibit a greater degree of leverage and therefore greater financial risk than 81.3 percent of industries. For example, most gas utility stocks today are selling below book value.

On behalf of the American Gas Association, I appreciate the opportunity to provide the gas utility industry's view on utility marketing practices and the role of utility diversification.

We urge this subcommittee to encourage utility competition in light of existing State regulation and the application of State and Federal laws that govern unfair competition.

[Mr. Zeigler's prepared statement with attachments follows:]

PREPARED STATEMENT OF CHARLES E. ZEIGLER, CHAIRMAN OF THE BOARD AND PRESIDENT, PUBLIC SERVICE CORPORATION OF NORTH CAROLINA, AND MEMBER, AMERICAN GAS ASSOCIATION

Good afternoon, I am Charles E. Zeigler, Chairman and President of Public Service Company of North Carolina, Inc. On behalf of the American Gas Association, I am pleased to appear before the Subcommittee. The American Gas Association (A.G.A.) is a national trade association comprised of nearly 300 natural gas distribution and transmission companies serving over 160 million consumers in all 50 states. Collectively, A.G.A. member companies account for nearly 85% of the nation's annual gas utility sales.

Natural gas currently provides about 27% of the energy consumed in the U.S. Gas is used in about 55% of all domestic residential and commercial establishments, and it provides 40% of the energy consumed by domestic industry, including agriculture. Almost all gas used in the U.S. is produced domestically, and natural gas provides two and one-half times as much end use energy to consumers as electricity. Thus, natural gas is a vital part of this country's energy mix.

Gas utilities have a significant role to play in providing their customers with gas utility service as efficiently as possible. To that end, gas utilities are involved in a variety of activities that have as their goal the efficient use of our natural resources.¹ Not all of these activities are directly related, in a strict sense, to the distribution of natural gas. Nevertheless, there is a legitimate justification for diversification into "non traditional" areas such as the sale and installation of gas appliances as well as devices or products that conserve energy.

Many non-utility activities are marketing-oriented, such as efforts to encourage the purchase (both directly from the utility and from independent contractors) of highly efficient gas appliances and heating and cooling equipment. In other instances, A.G.A. utility members cooperate with local code officials in assuring that gas service is not extended to new construction that does not comply with the energy efficiency and safety provisions of local codes and standards. Finally, most utilities are covered by the residential and commercial energy audit provisions contained in Titles II and VII of the National Energy Conservation Policy Act (NECPA)¹ as amended by the Energy Security Act.² This statute created the Residential Conservation Service (RCS) Program, which requires large utilities to offer energy

¹Pub. L. 95-619; 92 Stat. 3206; 42 U.S.C. §8201.

²Pub. L. 96-294; 94 Stat. 611; 42 U.S.C. §8211.

audits to eligible residential customers. It also created the Commercial and Apartment Conservation Service (CACS) Program, which is in its early stages of implementation.

Since the topic of this hearing is the competitive aspects of utility marketing practices, our testimony will discuss the respective competitive contexts of our activities mandated by NECPA, and the gas utility industry's diversification into various utility marketing activities, as well as into certain non-utility activities.

Voluntary and Mandatory Utility Diversification into Conservation and Other Marketing Activities

The natural gas utility industry has had an historical interest in energy conservation which predates the federal NECPA mandates and which had as its goal the preservation of existing gas markets through the most efficient use of natural gas. To illustrate this history, an A.G.A. survey made in August, 1978, (one year prior to the NECPA RCS mandate) revealed that 52% of the survey respondents³ provided residential energy audits, with 44% of the respondents providing the audits at no cost. Twenty-eight percent of these member companies sold attic insulation, 15% sold wall insulation and 5% marketed storm doors and windows. Many of these member companies offered financing of conservation measures at little or no interest. All of these programs promoted energy conservation for the ultimate benefit of utility customers, the utility, and gas appliance distributors.

³213 gas distribution companies were canvassed and 168 responded.

In the years prior to the Natural Gas Policy Act ("NGPA"), the natural gas industry's conservation efforts had security of supply as their goal. With the statutory elimination of the pre-NGPA supply uncertainties, the industry's conservation imperative changed dramatically, with today's efforts aimed at keeping the cost of energy at the lowest possible level in order to preserve our gas markets. The more efficiently gas is used, the lower its unit cost, and the less likely fuel switching is to occur. Encouraging energy conservation also enables our industry to flatten demand peaks, which benefits all of our customers. Thus, conservation is in our own self-interest, as well as in the interest of utility customers.

Most utilities are now prohibited by NECPA from selling and installing RCS Program measures, including those which are most effective at conserving energy (e.g., caulking and weatherstripping, insulation and storm windows and doors).⁴ However, some of the utility industry's pre-existing conservation marketing and installation programs were grandfathered from the NECPA prohibition and are still ongoing. Additionally, the application of these NECPA prohibitions have been waived for certain utilities whose supply or installation programs have been supported by their states' governors and have passed the FTC's

⁴§216 of NECPA prohibits the sale or installation of certain specified energy conservation measures by covered utilities. These measures include: caulking and weatherstripping; certain furnace efficiency modifications; ceiling, attic, wall and floor insulation; storm windows and doors; and active or passive solar equipment.

scrutiny concerning potential competitive impacts. Where this is the case, utilities are actively competing with small business contractors who also sell and install conservation measures.

While we do not believe that utility competition in these areas is unfair or anticompetitive by nature, we recognize that some contractors may perceive themselves to be at a disadvantage because of many misconceptions, including the notion that a utility is better able to compete because of its ability to cross subsidize its marketing activities through its ratebase. Not only is this misconception incorrect, it also ignores the increasing interest state regulators are taking in scrutinizing the diversification activities of utilities.

Some contractor groups testifying at a November 3, 1983, hearing before the Senate Small Business Committee suggested that utilities should not be allowed to diversify at all and intimated that many utility-related activities (such as appliance rebate programs) are anticompetitive. This just is not the case. Local regulatory commissions usually do not have jurisdiction to regulate non-utility activities per se; but they do have the authority to monitor these non-utility activities carefully, thereby helping to ensure against the utility's cross subsidization of non-utility activities through the ratebase. In addition to state regulatory commissions, state and federal antitrust laws provide protection from anticompetitive actions by utilities. We do not believe that a utility rebate program is any more anticompetitive than a rebate program offered by a competing appliance or equipment retailer.

A.G.A. believes that the "hidden agenda" in the efforts by

some to prohibit utility involvement in non-traditional marketing efforts is the fear of competition itself. In fact, the only logical rationale for such a prohibition is not to protect competition (thereby protecting consumers) but to protect utility competitors. This is contrary to the goal of the antitrust laws, which is to protect competition. There is no reason to believe that utilities are any more likely to behave in an anticompetitive manner than any other competitor in the supply and installation of energy conservation measures. Indeed, in examining the manner in which utilities were implementing the RCS Program, the Federal Trade Commission reported that it had "not yet found any evidence that these potential problems [regarding competition or consumer protection] have actually arisen."⁵

Finally, we must emphasize again that federal and state antitrust laws, as well as laws on unfair trade and consumer protection, provide ample safeguards to ensure that utility supply and installation activities are conducted fairly and competitively. To suggest, as some have, that utilities are inappropriate entrants in the markets addressed by NECPA is to penalize the consumer who would no longer be able to benefit from utility efforts. Competition produces the best products and services at the lowest possible prices. We submit that it would be a sad perversion of the system of antitrust laws to use a blanket prohibition to protect competitors from the workings of an inherently competitive system.

⁵Residential Conservation Service, Report of the FTC, Vol. I, at p. 5 (1982).

Some have also alleged that utilities are in a position to act anticompetitively because they are guaranteed a rate of return by their state regulatory commissions. Contrary to this claim, gas utilities are not guaranteed any rate of return. Rather, the state regulatory commission approves rates that are designed to afford the utility a reasonable opportunity to achieve its allowed rate of return.

Allowed revenues may fail to provide (after all costs) the earning of the allowed rate of return for many reasons, including unexpected business turnarounds, unanticipated regulatory developments, sales that fall below expected levels and unanticipated costs. Any or all of these factors can reduce the actual rate of return significantly below that allowed by the state regulatory commission. In fact, it is not uncommon for gas utilities to fall below the authorized rate of return.

Certainly, utilities are in a unique marketing position vis-a-vis the potential purchaser of conservation measures, who usually is, already, a utility customer. Despite any allegations of anticompetitive behavior, we do not believe that utilities can, under present law, or will abuse the relationship that they maintain with their customers. Utility customers who believe that their utility has abused the relationship can notify the state regulatory commission of their complaint.

In addition to the sale and installation of conservation measures, appliances and gas heating and cooling equipment, gas utilities provide another type of competition with private industry. In any given utility service area, there may be a number of private businesses that specialize in providing on-site

residential and/or commercial energy audits.

In this case, utility competition is primarily due to the manner in which utilities are required by statute to treat the costs of these audits. The direct cost to the utility customer for a residential audit performed by a utility under the federally mandated RCS Program is limited to a maximum of \$15. The excess utility cost for the audit above the maximum allowable charge to the customer is usually spread over all utility ratepayers.⁶ An A.G.A. survey shows that our members' average audit cost is \$128. Thus, the NECPA-mandated RCS Program audits, which cost the customer a statutory maximum of only \$15, would obviously be more attractive to the customer than a full cost audit provided by a private architect or heating and cooling contractor.

As we noted before, utilities were in the energy audit business for a long time prior to NECPA. This, coupled with the statutorily mandated subsidization of the audit cost above the \$15 maximum, can give utilities a competitive advantage in the energy audit business. We have never sought this advantage. This subsidization was mandated by Congress. In fact, A.G.A. has consistently argued against this subsidization since NECPA was in its legislative infancy; indeed, we strongly advocate repeal of both the RCS and the CACS Programs. We urge Congress to allow utilities to charge RCS Program participants the full cost of the audit.

⁶NECPA §§215(c)(1)(C) and 731(b)(3).

This remedy is the only one which would be satisfactory to utilities and to private business, and it would require amending NECPA. Nevertheless, it is only by allowing utilities to charge customers the full cost of the audit that private audit businesses will be able to compete effectively with utility audit programs.

Voluntary Marketing Practices and the Role of Utility Diversification

The gas utility industry is involved in a number of marketing activities, many of which are not, in the narrowest sense, directly related to providing gas utility service to its customers. These activities may be undertaken by the utility directly or through subsidiaries. While it would be disingenuous to suggest that these activities are pursued solely for conservation-related reasons, diversification provides significant benefits for utility customers as well as for utilities. Certainly, utility companies' efforts are not conducted in a manner which is indifferent to the utilities' primary customers.

The most familiar example of utility marketing efforts involves the sale of appliances and heating and cooling equipment. Through involvement in the sale of gas equipment, gas utilities promote the sale of gas. This is true even when the utility does not merchandise the equipment. In cases where the utility does market appliances and other equipment the gas utility usually does not offer the lowest prices.

Many non-marketing gas utilities advertise gas appliances and equipment generically to encourage gas sales. This type of promotion has obvious benefits for heating and cooling contractors

who might not be able to afford to push the sale of gas appliances and equipment on their own. In fact, utilities are very cognizant of the effects utility activities can have on small businesses. This is reflected by the active liaison most utilities maintain with local contractors, a liaison that includes educational programs to alert contractors to the latest local code requirements affecting equipment installation.

In some cases, non-utility merchandisers may not be large enough to service consumer demand. In addition, many contractors sell electric appliances as well as gas appliances and, thus, do not have the same level of interest in promoting gas equipment as does the gas utility industry. In any event, utility promotion of gas appliances provides obvious benefits for those who market gas appliances (i.e., both utilities and small businesses), as well as for non-merchandising gas utilities.

In addition to competing with small businesses in the sale and installation of appliances and other consumer goods, utilities provide service calls to consumers whose gas appliances or equipment need repair. Often, these calls are not emergencies and are made as a service to utility customers. However, there are a number of instances in which utilities provide true emergency services for their customers, such as responding to calls concerning suspected gas leaks. Providing these safety calls is a vital part of the industry's interest in preventing damages that can result from undetected or unrepaired gas leaks and faulty equipment. Although this type of safety service can be performed by non-utility businesses, in many instances, the gas utility may be the only source for this emergency assistance. In fact, most

utilities maintain 24-hour service capability, a service most contractors are ill-equipped to provide. In any case, utilities will continue to provide safety-related programs as a service to their customers and to ensure a level of service commensurate with the interest of public safety.

Some utilities are involved in federally approved research, development and promotion of new energy technologies and other proprietary efforts, such as cogeneration and natural gas vehicles. Despite the nature of these and other types of diversification, there are three main reasons gas utilities seek to diversify:

(1) To preserve and expand gas markets -- Gas utilities are involved in merchandising gas appliances and equipment, are conducting energy conservation programs and are entering into marketing projects such as jointly-owned user/utility cogeneration facilities, low Btu on-site gasification facilities, and natural gas powered vehicles. If a utility is able to market gas effectively and thereby increase the number of customers it serves, it will decrease the percentage of fixed costs each customer will be paying. These efforts allow utilities to strengthen the gas market effectively for all customers.

(2) To secure present and future gas supplies -- Gas utilities increased their efforts in energy exploration and production, coal gasification and other supply projects during the 1970s when the estimates of future gas supplies were less optimistic than they are now. These operations have proven quite successful in helping to alleviate gas supply uncertainties.

(3) To improve financial stability -- A.G.A. member companies strongly believe that diversification is needed to enhance their financial strength. Diversification helps counter the effects of business seasonality and regulatory lag by stabilizing a company's profits. Furthermore, it can help maintain or expand gas markets, thereby enhancing utility operations. Financially stronger gas companies are more capable of providing gas service to their customers.

Diversification also allows companies to expand into areas that have a growth potential, which is not always possible in the

utility business. Improved financial stability and strength should lower the company's cost of capital, thereby saving money for gas consumers.

An A.G.A. financial analysis released in June, 1983 (Exhibit I),⁷ analyzed the changes in investment risk for the regulated natural gas industry. The study points out that in:

. . . recent years a number of factors have been considered as generally responsible for increased risk in the gas industry. These include rising gas costs, inflation, fluctuating interest rates, increased competition, and regulatory conditions.⁸

During the past ten years, total investment risk for companies primarily engaged in the distribution of natural gas has increased both absolutely and relative to other industries. According to the A.G.A. study, "on an absolute basis, risk as measured by the variability in earnings in terms of return on net worth increased for both pipelines and distributors between 1972 and 1976 and 1977-1981."⁹ Furthermore, as measured by debt/equity ratios, relative risk was also reflected in the study, which showed that, in 1982, "distribution companies exhibited a greater degree of leverage (and, therefore greater financial risk) than 81.3 percent of industries. . . ."¹⁰

⁷Financial Analysis: The Changing Nature of Investment Risk for the Natural Gas Industry, American Gas Association (Arlington, Virginia, June 1983), FA 83-3.

⁸Id., at 1.

⁹Id., at 2.

¹⁰Id., at 3.

This conclusion contradicts the generally held assumption that regulated gas utilities are of relatively low risk. While that may have been true in the past, it is not so now. As the A.G.A. study points out:

[f]ailure of those maintaining oversight of the earnings of the regulated gas industries to acknowledge the increased risk will result in greater difficulty in attracting capital at a competitive and reasonable cost. Inability to attract capital on comparable terms with other industries . . . will result, in the long run, in higher rates to the consumer.¹¹

Thus, contrary to the claims of some, diversification will assist in lowering -- not raising -- the risk of investment in gas utility stock.

The National Association of Regulatory Utility Commissioners (NARUC) last year published its 1982 Report of the Ad Hoc Committee on Utility Diversification.¹² In discussing gas utility diversification, the Report described it as having:

. . . a historical record which shows that it [diversification] is not something recently sought as a means to escape financial trouble, but really was a natural process by which gas utilities sought to achieve or maintain financial health.¹³

¹¹Id., at 11.

¹²1982 Report of the Ad Hoc Committee on Utility Diversification, National Association of Regulatory Utility Commissioners (Washington, D.C., 1982).

¹³Id., at 32.

While the NARUC Report did not endorse utility diversification without qualification, it did agree that there are many legitimate reasons that can justify diversification by a utility into areas both functionally and non-functionally related.¹⁴ Among those reasons, NARUC cited the need for supplemental sources of supply, developing and maintaining markets and protecting shareholders' investment.¹⁵

A.G.A.'s Position on Proposed Alternatives to Utility Competition

Several witnesses at the previously mentioned Senate Small Business Committee hearing proposed additional restrictions on utility competition. Frank Swain, Chief Counsel for Advocacy of the Small Business Administration, stated them in his oral presentation as follows:

- DOE and FTC should provide the states with guidelines for use in assessing the issue of utility subsidization.
- DOE should closely scrutinize (and encourage public participation in consideration of) utility applications for waivers of NECPA's prohibition on utility supply and installation of RCS Program measures.
- State utility commissions should have jurisdiction over non-utility ventures in order to address the issues arising from utility competition (such as allegations of cross subsidization).

¹⁴Id., at 34, 35.

¹⁵Id., at 35.

Witnesses from the contracting community echoed the SBA suggestions and went on to support an outright ban on utility competition.

A.G.A.'s views on these proposals are as follows:

- Federal Guidelines -- There is a role for federal consideration of this issue. However, with regard to utility competition, NECPA requires that DOE's RCS and CACS Program regulations address anticompetitive aspects of utility competition, specifically as regards supply and installation of Program measures. The NARUC diversification study sets out factors that state regulators should consider in addressing the cross subsidization issue. Consequently, we believe that there are already ample sources for state guidance.
- DOE's NECPA Waiver Process -- There is nothing in NECPA that prevents public participation in the consideration of utility waiver applications. Furthermore, DOE is required by NECPA to consider potential anticompetitive impact of any such application. Consequently, we do not believe that any additional federal legislative or regulatory action is necessary.
- Expansion of State Regulatory Commission Jurisdiction Over Utility Competition -- States already have jurisdiction over any potential anticompetitive aspects of utility activities, although this authority usually resides in state agencies other than the PUC. Nevertheless, the PUC can regulate non-utility activities to the extent that such activities affect utility operations. Thus, any potential for utility cross subsidization is subject to PUC scrutiny and control.
- Banning Utility Competition -- As we have stated before, utilities have legitimate and pressing reasons for diversifying into non-utility activities. Furthermore, ample safeguards exist in state and federal law to protect small businesses from any potential anticompetitive activities by utilities.

Thus, A.G.A. believes that the alternatives proposed last November by SBA and supported by the contractor groups are unnecessary and injurious to the utilities' ability to serve the legitimate interests of their customers. We urge this Subcommittee not to support any of them.

Conclusion

The American Gas Association appreciates the opportunity to provide the gas utility industry's views on utility marketing practices and the proper role of diversification. We urge this Subcommittee to encourage utility competition in light of existing state regulation and the application of state and federal laws governing unfair competition.



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THE CHANGING NATURE OF INVESTMENT RISK FOR THE NATURAL GAS INDUSTRY

A. Introduction

In evaluating the reasonableness of rate increases filed by investor-owned regulated entities, critical attention is paid by regulators to the firm's cost of capital. The regulated entity competes for capital in a market with all enterprises (both regulated and non-regulated), and thus, in order for the company to attract capital it must provide an investor the expectation of earning a return comparable with that available from other investment alternatives (depending upon relative degrees of risk).

It is axiomatic that the return required by investors is related to the degree of risk in the investment. Therefore, in setting an allowed rate of return for a regulated gas company, regulators must be necessarily concerned with the relative riskiness of the investment in relation to that of alternative investments. In many instances, particularly in the natural gas industry, the regulated company has been assumed to be of a relatively lower risk (in relation to nonregulated business) because it is considered to be a natural monopoly -- an entity not subject to the vagaries of competition.

In recent years a number of factors have been considered as generally responsible for increased risk in the gas industry. These include rising gas costs, inflation, fluctuating interest rates, increased competition, and regulatory conditions. This analysis examines the relative degree of investment risk for companies primarily engaged in the transmission and/or distribution of natural gas. While investors generally examine a variety of factors when making an investment decision, and rating agencies evaluate numerous criteria in determining the rating of a particular fixed income instrument, for purposes of this analysis, investment risk (consisting of both business and financial risk) is measured primarily in terms of volatility of earnings. Debt/equity ratios (degree of leverage) are also examined. Changes in the nature of risk over the 10-year period 1972-1981 are examined and comparisons of the relative degree of risk for regulated gas companies with that of many major industry groupings are developed.

B. Executive Summary

- o As a result of changing market conditions and industry cost structure, rising interest rates, inflation, and regulatory conditions, total investment risk for companies primarily engaged in the transmission and/or distribution of natural gas has increased both absolutely and relative to other industries during the past 10 years. Therefore, so that regulated gas companies may remain competitive in the capital markets, cost of capital determinations must reflect the changing nature of risk.
- o On a relative basis, Table 1 details the change in investment risk (as measured by variability in earnings) for the regulated gas industries.
 - Whereas in the 1972-1976 period 3.8 percent of regulated and nonregulated industries exhibited less variability in return on total capital than the gas distribution industry, by the 1977-1981 period 28.3 percent exhibited less volatility.
 - Similarly, in the 1972-1976 period, 30.2 percent of industries exhibited less variability in earnings (as measured by return on total capital) than the gas transmission industry; however, by 1977-1981 the pipeline industry had greater variability (and therefore greater business risk) than 47.2 percent of industries.
 - In terms of variability in return on net worth, in the 1972-1976 period, 9.6 percent of industries exhibited less risk than distribution companies; however, by the 1977-1981 period the distribution industry's earnings reflected a greater degree of variability than 51.9 percent of industries.
 - The relative business risk of pipelines as measured by variability in return on net worth increased from being riskier than 13.5 percent of industries in the 1972-1976 period to 32.7 percent of industries in the 1977-1981 period.
- o On an absolute basis, risk as measured by the variability in earnings in terms of return on net worth increased for both pipelines and distributors between 1972-1976 and 1977-1981.

- o Financial risk as measured by debt/equity ratios declined somewhat on an absolute basis between 1972-1976 and 1977-1981; however, on a relative basis, in 1982, distribution companies exhibited a greater degree of leverage (and, therefore, greater financial risk) than 81.3 percent of industries while pipelines exhibited greater financial risk than 68.8 percent of industries.

C. Background

The earnings of all regulated companies, regardless of industry, are subject to evaluation under the same general legal principles. In the Bluefield Waterworks case, the Supreme Court stated:

"A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. The return should be reasonably sufficient to assure confidence in the financial soundness of the utility, and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties."¹ (emphasis added)

¹ Bluefield Waterworks & Improvements Co. v. Public Service Commission of West Virginia, 262 U.S. 679, 692-695 (1923).

In the Hope Natural Gas decision, the Court stated:

"The return to the equity owner shall be commensurate with returns on investments in other enterprises having corresponding risk. That return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital."² (emphasis added)

Inherent in both of these legal decisions is the concept of "comparability." That is, investors in regulated enterprises require a return on their investment comparable to that attainable from investments in other industries (or money market instruments). This is the implicit assumption of the capital attraction standard as enunciated in the legal principles - that the regulated entity must be able to attract capital so that it may function on a long-term basis. In order to attract the necessary capital, the company must be able to offer its investors a return equivalent to that available from alternative investments.

Underlying the concepts of comparability and capital attraction is the notion of investment risk. There is an axiom in economics and finance that investors in industries (or money market instruments) that exhibit a relatively higher degree of risk require a higher rate of return than do investors in opportunities exhibiting a relatively lower degree of risk. In general, investors are assumed to be risk-averse. In other words, for a given return level, investors prefer the investment with the least risk.

Risk, in the context of investment analysis, is present whenever there is a probability distribution of possible outcomes rather than a certain outcome. Normally, an investor is not sure what his return will be in an equity investment, but he can gain some knowledge of the probable return by examining the past behavior of the return received from the investment, the financial leverage of the firm, the performance of the firm and industry, and general appraisals of future growth.

Total investment risk consists of two interrelated components, business risk and financial risk. Financial risk can be estimated by examining the capital structure of the firm and

²Federal Power Commission v. Hope Natural Gas Co. 320 U.S. 591, 603 (1944).

hypothesizing that the greater the percentage of debt, and the more expensive it is, (i.e., the higher the embedded cost of debt) the more volatile is the return on equity. Traditionally, the view has been held that an equity investor is subject to more risk in a highly-leveraged company than he is in one employing a lesser degree of leverage. The reasons for this are twofold. First, a more leveraged company has a larger amount of fixed charges (i.e., interest payments), and if earnings decline, is more susceptible to financial problems. Hence, there is increased risk for the equity holder. Second, the firm does not have the contractual obligations with equity holders that it has with fixed income security holders, and consequently, should liquidation occur, the common equity holders are last in the priority of claims.

Business risk is measured in terms of fluctuations in earnings. Higher fluctuations in earnings are symptomatic of higher levels of risk to the investor. The tighter the distribution of possible outcomes (the less variation in earnings), the more likely the actual outcome will equal the expected outcome, and, therefore, the more certain is the return on the investment. Investors, therefore, will typically require a lower rate of return from a firm that has less variation in its earnings than they would from a firm with a more volatile earnings pattern.

Traditionally, the relative degrees of business and financial risk have been interrelated. That is, companies (industries) with a high degree of business risk (higher variability of earnings) would be expected to have a lesser degree of financial risk (a lower percentage of debt in the capital structure). Utilities (electric, gas, water, and telephone) traditionally have had relatively higher levels of debt in their capital structure than other industries, and consequently have had higher levels of financial risk, offset by lower levels of business risk.

D. Methodology

To determine levels of business risk, historical financial data on over 50 industries were developed from the Value Line Investment Survey. Similar data for the gas distribution and transmission industries were developed from A.G.A.'s Gas Facts. The assessment of business risk was conducted through an examination of variability in profitability ratios. Profitability ratios for which data were derived are return on total capital and return on net worth. Return on total capital is defined as

$$\frac{\text{Net Income} + (1 - \text{tax rate}) \text{Interest on Long-Term Debt}}{\text{Long-Term Debt} + \text{Net Worth (Less deferred taxes)}}$$

The return on total capital ratio is a principal measure of the economic performance of a firm, or industry, since it does not reflect distortions among industries that may occur as a result of differences in capital structures, and does reflect a relationship between income and the total capital (provided by all investors) used to generate that income.

Return on net worth is expressed as

$$\frac{\text{Net Income}}{\text{Net Worth}}$$

where net worth is considered to include all of the company's (industry's) assets less current liabilities, long-term debt, and all other noncurrent liabilities. Net worth can be considered as the sum of common and preferred stockholders' equity. The Value Line Investment Survey does not publish data on return on equity for all of its industry groupings, therefore, this standard profitability measure has not been evaluated in this analysis. However, as a general principle, return on net worth can be considered an adequate proxy for return on equity.

For each of these data series, information covering the period 1972-1981 was collected. Various statistical measures were used to examine the variability of the profitability data over each time period and among industry groupings.

The coefficient of variation was utilized to reflect the relative variation in both return on total capital and return on net worth. The coefficient of variation is a measure that expresses the size of the variation relative to the size of the quantity being measured. This measure reveals the degree of instability per percentage point of return. It reflects, therefore, a risk/return tradeoff. The coefficient of variation is calculated by expressing the standard deviation as a percent of the mean. As a measure of risk, a recent study found that investment bankers placed their highest level of confidence, importance, and significance on the coefficient of variation, in relation to other measures of risk.³ The following is an example of the usefulness of the coefficient of variation:

1. The 10-year average rate of return on total capital for Industry A is 13 percent, with a standard deviation of 2.
2. The 10-year average rate of return on total capital for Industry B is 15 percent, but also with a standard deviation of 2.

³P.R. Chandrasekaran and William P. Dukes, "Risk Variables Affecting Rate of Return of Public Utilities." Public Utilities Fortnightly, February 26, 1981, p. 34.

3. Since the coefficient of variation is the standard deviation as a percentage of the mean, the coefficient of variation for Industry A is $2/13$ or .154 and for Industry B, it is $2/15$ or .133. Thus, for the two industries, each of which has the same standard deviation, the industry with the lower rate of return has the higher coefficient of variation, which means that it would have a more difficult time attracting capital. Industry B, with the same level of volatility as Industry A, offers a higher return and, thus, has a lower coefficient of variation. Consequently, it will have a better opportunity for attracting capital.

The standard deviation and the variance were utilized as additional measures of variability in terms of return on net worth and return on total capital. The standard deviation measures the average amount by which a set of individual data varies in either direction from its mean. The variance, which was listed by investment bankers as second to the coefficient of variation as a measure of business risk, is calculated by squaring the standard deviation.

Data on the degree of leverage (debt/equity portions of the capital structure) for use in evaluating the level of financial risk were derived from Forbes in addition to Gas Facts.

E. Discussion of Results

There are various means of measuring the relative risk of a firm or industry. The regulated gas industry has faced relative risks in previous years in terms of supply shortages and high degrees of leverage. However, regulated gas companies have historically exhibited a relatively low degree of business risk (as measured solely by earnings volatility) in comparison with nonregulated industries. As Tables 2-5 (attached) indicate however, in recent years the earnings volatility of regulated gas companies has increased and consequently, the nature of risk faced by these companies has changed.

Tables 2 and 3 provide data on the variability in return on total capital for 53 industries during the 1972-1981 period. Variability in return on total capital is generally accepted as a measure of the total business risk of the enterprise. That is, it measures the total risk of the firm before taking into account the effects of leverage on the risks borne by the stockholders.

As Table 2 indicates, during 1972-1976 gas distribution companies ranked 51 out of 53 industries. Clearly, distribution companies were among the least risky industries (as measured by earnings volatility) surpassed only by the household products industry and the health care/hospital supplies industry. Thus, there has been a perception that regulated gas companies were among the least risky industries with stable earnings flows. In fact, in 1972-1976 over 94 percent of industries were riskier than

the gas distribution industry. By examining the standard deviation and the variance, it can be seen that only the health care/hospital supplies industry was less risky during the period. However, comparing Tables 2 and 3 it can be seen that during 1977-1981 the coefficient of variation of gas distribution companies rose from .0374 to .0613, and since many other industries experienced less volatility in earnings during the period, gas distributors moved from 51st out of 53 industries to 38th out of 53. So that by the 1977-1981 period distribution companies were riskier than 28.3 percent of industries--including such cyclical industries as electrical equipment and machinery.

The increased risk of distribution companies is evidenced by the fact that of 53 industries, the variability in return on total capital declined for 40 groups between 1972-1976 and 1977-1981, with only 13 (24.5 percent) industries increasing - one of which was the gas distribution industry.

For the gas pipeline industry, the relative variability of earnings as measured by return on total capital declined slightly from the 1972-1976 period to the 1977-1981 period; however, the industry became noticeably riskier in relation to other industries over the two time periods. Whereas pipelines ranked 37th out of 53 industries in 1971-1976, by 1977-1981 the industry was 28th out of 53.

Tables 4 and 5 provide data on the return on net worth for 52 industries during the 1972-1981 period. In this analysis, return on net worth is used as a proxy for return on equity (ROE) since the Value Line Investment Survey does not provide ROE data for each of its industry groupings. As Table 4 indicates, using the coefficient of variation, natural gas distribution companies ranked 47th out of 52 industries during the 1972-1976 period. In other words, the variability of earnings for the industry, as measured by return on net worth, was so low that only five other industries had less variation. In terms of both their standard deviation and variance, only four industries had less variability than the gas distribution industry during the period.

However, as Table 5 indicates, the distribution industry's level of risk changed dramatically during the 1977-1981 period. The coefficient of variation increased from .0479 to .1000. During the five-year period (the most recent period for which full-year financial data are available), the distribution industry's ranking went from 47th out of 52 to 25th out of 52. In other words, during 1972-1976 only five other industries were less risky than the distribution industry, but during the 1977-1981 period, 27 other industries were less risky. In the earlier period the distribution industry was less risky than 89 percent of industries. During the most recent period, the industry was less

risky than only 46 percent of industries. In fact, during 1977-1981 more than one-half of the industry groups surveyed were less risky than the distribution companies. Similar rankings are found when risk is measured by either standard deviation or variance.

While the movement in ranking by the gas distribution industry during the two time periods was substantial, equally as important was how the distribution industry fared in comparison with other industries. By comparing Tables 4 and 5, it can be seen that 28 industries became relatively riskier during the most recent period. However, of the 28, only two industries -- railroad equipment and original equipment auto parts -- moved more slots in the risk rankings than the gas distribution industry did.

On an absolute basis, only 16 of the 52 industries registered increased variability of earnings between the two periods. As Tables 4 and 5 reflect, two of the 16 industries suffering increased variability -- and, consequently, increased risk -- were natural gas distributors and pipelines.

For natural gas pipelines, the relative change in variability was not as dramatic as it was for distributors; however, there was a noticeable change in the pipelines' risk. From the 1972-1976 period to the 1977-1981 period, the pipelines' coefficient of variation rose from .0578 to .0728. During the 1972-1976 period, pipelines ranked 45th out of 52 industries in terms of variability of earnings, i.e., only 13.5 percent of industries surveyed were less risky. This again lends credence to the argument that pipelines were among the least risky of industries. As Table 5 indicates, during the 1977-1981 period pipelines became the 35th most risky industry -- almost 33 percent of industries were less risky than pipelines during the period. Thus, for the pipelines, as well as the distributors, the nature of risk changed sharply from the first period to the later period.

In terms of financial risk, Tables 6 and 7 present data on the relative degree of leverage for 48 industries. As the tables indicate, for both periods, 1974 and 1982, gas distributors and pipelines have historically exhibited a relatively higher degree of leverage than other industries. There are a number of reasons for this; namely, the historically lower business risk as reflected in stable earnings patterns and the capital intensity of the industries.

As Table 6 indicates, in 1974 about 90 percent of all industries exhibited a lower degree of financial risk than the gas distribution industry. Over 83 percent of industries had a lower degree of financial risk than the gas pipeline industry. The only industries exhibiting greater leverage than the regulated gas industries in 1974 were airlines, telecommunication, electric utilities, and financial services. By 1982, however, while the absolute level of financial risk declined for both the distribution and pipeline industries (Table 7), the relative degree of risk did

not change substantially. Over 81 percent of industries exhibited a lower degree of financial risk than the distribution industry, while close to 70 percent of industries exhibited less financial risk than the pipelines.

As the attached tables indicate, the level of risk for the regulated gas industries has increased from the 1972-1976 period to the 1977-1981 period. The increased risk measured primarily in terms of variability of earnings has resulted from a number of factors. Conditions generally considered to be responsible for the increased risk include the rising cost of gas⁴ which reduces the ability of the regulated gas industries to adapt to changing competitive conditions (conditions which have been changing dramatically), inflation, fluctuating interest rates and changing regulatory conditions. To the extent that these factors will continue in the future, the industries' level of risk can be expected to increase further.

F. Conclusions

Regulated industries must compete with all industries, both regulated and nonregulated, in the capital markets. In order to attract capital to maintain their financial health, the natural gas distribution and transmission companies must be able to offer a return to investors commensurate with the relative risk of their investment. Historically, in comparison with nonregulated industries, the regulated natural gas companies have been assumed to be of relatively low risk because of their stable earnings patterns. This analysis has shown that these companies did in fact have relatively stable earnings patterns during the 1972-1976 period (although the companies faced risks of a different nature -- in terms of supply shortages, high degrees of leverage, etc.) However, this analysis finds that the nature of risk for the regulated gas industries has changed. Table 1 reflects the extent to which many other industries are less risky than the gas distribution and transmission industries. As the table shows, the relative business risk of the regulated gas industries increased sharply from the 1972-1976 period to the 1977-1981 periods. In comparison with the regulated gas industries, many more industries exhibited less variability in earnings (business risk) in the latter period. In terms of degree of leverage (financial risk) during the 1974-1982 period the regulated gas industries continued to exhibit greater financial risk than many industries. Thus, the gas distribution and transmission industries today exhibit relatively greater overall investment risk than in previous periods, necessitating cost of capital adjustments that reflect these changed conditions.

⁴A recent A.G.A. study found that costs under the control of the regulated gas industry declined as a percentage of the average retail gas price from 49 percent in 1971 to only 28 percent in 1981. See "Cost Components of the Average Gas Price," American Gas Association, (March 4, 1983), p. 1.

Failure of those maintaining oversight of the earnings of the regulated gas industries to acknowledge the increased risk will result in greater difficulty in attracting capital at a competitive and reasonable cost. Inability to attract capital on comparable terms with other industries competing in the capital markets will result, in the long run, in higher rates to the consumer.

TABLE 1

SUMMARY TABLE

CHANGES IN RELATIVE INVESTMENT RISK FOR
GAS DISTRIBUTION AND PIPELINE INDUSTRIES

<u>Risk Measure</u>	<u>Distribution Industry</u>	<u>Pipeline Industry</u>
	<u>% of Industries Exhibiting Less Risk</u>	
Variability of Return on Total Capital		
1972 - 1976	3.8	30.2
1977 - 1981	28.3	47.2
Variability of Return on Net Worth		
1972 - 1976	9.6	13.5
1977 - 1981	51.9	32.7
Debt/Equity Ratio		
1974	89.6	81.3
1982	81.3	68.8

Sources: Value Line Investment Survey and A.G.A. Gas Facts

TABLE 2
VARIABILITY IN RETURN ON TOTAL CAPITAL¹
1972 - 1976

(Ranked by Coefficient of Variation)

<u>Industry</u>	<u>Coefficient of Variation²</u>	<u>Standard Deviation³</u>	<u>Variance³</u>	<u>Average Rate of Return</u>
1. Real Estate	.5468	2.7447	7.5330	5.02
2. Toys & School Supplies	.4503	3.7733	14.2376	8.38
3. Coal/Uranium/Geothermal	.4793	6.4896	42.1144	13.54
4. Sugar	.4435	4.5504	20.7064	10.26
5. Maritime	.4028	2.4653	6.0776	6.12
6. Steel (General)	.3220	3.1492	9.9176	9.78
7. Steel (Integrated)	.3207	2.4441	5.9736	7.62
8. Oilfield Services/Equipment	.2267	2.7614	7.6256	12.18
9. Home Appliances	.2107	2.2042	4.8584	10.46
10. Textiles	.2081	1.2280	1.5080	5.90
11. Metal Fabricating	.2078	1.7165	2.9464	8.26
12. Grocery Store	.2055	1.4959	2.2376	7.28
13. Electrical Equipment	.2025	2.0455	4.1840	10.10
14. Retail (Special Lines)	.1868	2.1039	4.4264	11.26
15. Paper & Forest Products	.1834	1.8051	3.2584	9.84
16. Advertising	.1767	2.5483	6.4936	14.42
17. Broadcasting/Cable TV	.1688	2.0655	4.2664	12.24
18. Apparel	.1629	1.1792	1.3904	7.24
19. Machinery	.1601	1.7607	3.1000	11.00
20. Precision Instruments	.1585	1.7314	2.9976	10.92
21. Aerospace	.1497	1.2816	1.6424	8.56
22. Chemical (Specialty)	.1470	1.5025	2.2576	10.22
23. Trucking & Transport Leasing	.1436	1.8691	3.4936	13.02
24. Medical Services	.1423	.8424	.7096	5.92
25. Auto Parts (Replacement)	.1355	1.3764	1.8944	10.16
26. Tire & Rubber	.1326	.9550	.9120	7.20
27. Electronics	.1296	1.4051	1.9744	10.84
28. Auto Parts (Original Equipment)	.1263	1.3063	1.7064	10.34
29. Brewing	.1218	1.0911	1.1904	8.96
30. Chemical (Basic)	.1205	1.3185	1.7384	10.94
31. Retail Stores	.1190	1.1089	1.2296	9.32

Table 2 (Continued)

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Industry	Coefficient of Variation ²	Standard Deviation ³	Variance ³	Average Rate of Return
32. Building	.1160	.9887	.9776	8.52
33. Industrial Services	.1134	1.0365	1.0744	9.14
34. Shoe	.1098	1.2784	1.6344	11.64
35. Machine Tool	.1062	.8602	.7400	8.10
36. Packaging & Containers	.1016	.9432	.8896	9.28
37. NATURAL GAS PIPELINES ⁴	.1005	.9038	.8169	8.99
38. Drugstore	.0910	1.0088	1.0176	11.08
39. Newspaper	.0893	1.1289	1.2744	12.64
40. Finance	.0766	.5913	.3496	7.72
41. Soft Drink	.0718	1.2066	1.4560	16.80
42. Food Processing	.0683	.7239	.5240	10.60
43. Publishing	.0676	.6356	.4040	9.40
44. Multiform	.0643	.4690	.2200	7.30
45. Railroad Equipment	.0607	.4858	.2360	8.00
46. Toiletries/Cosmetics	.0589	.9826	.9656	16.68
47. Fast Food	.0524	.6375	.4064	12.16
48. Drug (Ethical)	.0529	.8754	.7664	16.54
49. Telecommunications	.0458	.3007	.0904	6.56
50. Drug (Proprietary)	.0403	.6615	.4376	16.42
51. NATURAL GAS DISTRIBUTORS ⁴	.0374	.2674	.0715	7.15
52. Household Products	.0283	.3763	.1416	13.32
53. Health Care/Hospital Supplies	.0134	.1625	.0264	12.16

¹Return on Total Capital is defined as:

$$\frac{\text{Net Income} + (1 - \text{tax rate}) \text{Interest on Long-Term Debt}}{\text{Long-Term Debt} + \text{Net Worth (less deferred taxes)}}$$

²The coefficient of variation is a measure of relative variation of a series of data, i.e., a measure that expresses the size of the variation relative to the size of the quantity being measured. The coefficient expresses the degree of instability per percentage point of return.

³The standard deviation expresses variation in terms of the distances (deviations) by which the various numbers depart from the mean. The variance is calculated by squaring the deviations and then averaging their squares. The square root of the variance is the standard deviation. Neither the standard deviation nor the variance provides information as to relative variability.

⁴Gas industry data derived from A.G.A. Gas Facts, various issues.

Source: Value Line Investment Survey, various issues, except as noted.

TABLE 3
 VARIABILITY IN RETURN ON TOTAL CAPITAL¹
 1977 - 1981
 (Ranked by Coefficient of Variation)

<u>Industry</u>	<u>Coefficient of Variation</u> ²	<u>Standard Deviation</u> ³	<u>Variance</u> ³	<u>Average Rate of Return</u>
1. Sugar	.5331	4.3287	18.7376	8.12
2. Steel (Integrated)	.3962	2.2583	5.1000	5.70
3. Tire & Rubber	.2915	1.7025	2.8985	5.84
4. Steel (General)	.2759	3.2006	10.244	11.60
5. Auto Parts (Original Equip.)	.2454	2.6158	2.9118	10.66
6. Textiles	.2365	1.5513	2.4065	6.56
7. Metal Fabricating	.1617	2.0209	4.0840	12.50
8. Real Estate	.1597	.9899	.9800	6.20
9. Finance	.1547	1.1977	.3996	7.74
10. Broadcasting/Cable TV	.1538	1.9712	3.8856	12.82
11. Paper & Forest Products	.1536	1.6092	2.5896	10.48
12. Apparel	.1533	1.6620	2.7624	10.84
13. Oilfield Services/Equipment	.1513	2.3004	5.2920	15.20
14. Railroad Equipment	.1372	1.2563	1.5784	9.16
15. Multiform	.1352	1.2464	1.5536	9.22
16. Machine Tool	.1320	1.7532	3.0736	13.28
17. Building	.1306	1.3711	1.8800	10.50
18. Coal/Uranium/Geothermal	.1239	1.1496	1.3216	9.28
19. Home Appliances	.1231	1.4302	2.0456	11.62
20. Advertising	.1151	2.1602	4.6664	18.76
21. Toys & School Supplies	.1141	1.4511	2.1056	12.72
22. Trucking & Transport Leasing	.1102	1.5761	2.4840	14.30
23. Electronics	.1102	1.3485	1.8184	12.24
24. Auto Parts (Replacement)	.1081	1.2000	1.4400	11.10
25. Industrial Services	.1046	1.2909	1.6664	12.34
26. Chemical (Specialty)	.0964	1.2703	1.6136	13.18
27. Retail Stores	.0958	.9086	.8256	9.48
28. NATURAL GAS PIPELINES ⁴	.0934	1.1239	1.2631	12.03
29. Health Care/Hospital Supplies	.0925	1.2548	1.5744	13.56
30. Brewing	.0813	.8050	.6480	9.90
31. Precision Instruments	.0790	1.1412	1.3024	14.44

Table 3 (Continued)
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Industry	Coefficient of Variation ²	Standard Deviation ³	Variance ³	Average Rate of Return
32. Chemical (Basic)	.0786	.8065	.6504	10.26
33. Aerospace	.0785	1.0557	1.1144	13.44
34. Maritime	.0733	.7859	.6176	10.72
35. Retail (Special Lines)	.0651	.8841	.7816	13.58
36. Grocery Store	.0640	.5352	.2864	8.36
37. Medical Services	.0639	.5851	.3424	9.16
38. NATURAL GAS DISTRIBUTORS ⁴	.0613	.5645	.3187	9.21
39. Newspaper	.0590	.9453	.8936	16.02
40. Toiletries/Cosmetics	.0490	.8163	.6664	16.66
41. Packaging & Containers	.0483	.4167	.1736	8.62
42. Electrical Equipment	.0461	.6957	.4840	15.10
43. Drug (Ethical)	.0440	.7211	.5200	16.40
44. Machinery	.0432	.5463	.2984	12.64
45. Telecommunications	.0424	.3347	.1120	7.90
46. Drug (Proprietary)	.0415	.7031	.4944	16.94
47. Publishing	.0377	.5115	.2616	13.58
48. Drugstore	.0326	.4427	.1960	13.60
49. Fast Food	.0285	.3544	.1256	12.42
50. Soft Drink	.0265	.4604	.2120	17.40
51. Household Products	.0204	.2871	.0824	14.06
52. Shoe	.0159	.2191	.0480	13.80
53. Food Processing	.0149	.1744	.0304	11.74

¹Return on Total Capital is defined as:

$$\frac{\text{Net Income} + (1 - \text{tax rate}) \text{Interest on Long-Term Debt}}{\text{Long-Term Debt} + \text{Net Worth (less deferred taxes)}}$$

²The coefficient of variation is a measure of relative variation of a series of data, i.e., a measure that expresses the size of the variation relative to the size of the quantity being measured. The coefficient of variation expresses the degree of instability per percentage point of return.

³The standard deviation expresses variation in terms of the distances (deviations) by which the various numbers depart from the mean. The variance is calculated by squaring the deviations and then averaging their squares. The square root of the variance is the standard deviation. Neither the standard deviation nor the variance provides information as to relative variability.

⁴Gas industry data derived from A.G.A. Gas Facts, various issues.

Source: Value Line Investment Survey, various issues, except as noted.

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TABLE 4
VARIABILITY IN RETURN ON NET WORTH¹
1972 - 1976
(Ranked by Coefficient of Variation)

<u>Industry</u>	<u>Coefficient of Variation²</u>	<u>Standard Deviation³</u>	<u>Variance³</u>	<u>Average Rate of Return</u>
1. Maritime	.5387	6.1089	37.3184	11.34
2. Toys & School Supplies	.5351	5.1694	26.7224	9.66
3. Coal/Uranium/Geothermal	.4708	9.0307	81.5536	19.18
4. Sugar	.4534	6.0487	36.5864	13.34
5. Steel (Integrated)	.3333	3.0997	9.6080	9.30
6. Steel (General)	.3307	3.9154	15.3304	11.84
7. Textiles	.2507	1.7600	3.0976	7.02
8. Grocery Store	.2374	2.0605	4.2456	8.68
9. Oilfield Services/Equipment	.2349	3.7860	14.3336	16.12
10. Metal Fabricating	.2307	2.4916	6.2080	10.80
11. Home Appliances	.2226	2.7781	7.7176	12.48
12. Electrical Equipment	.2091	2.6265	6.8984	12.56
13. Paper & Forest Products	.1954	2.6374	6.9560	13.50
14. Apparel	.1778	1.5396	2.3704	8.66
15. Machinery	.1777	2.4919	6.2096	14.02
16. Medical Services	.1770	1.8478	3.4144	10.44
17. Advertising	.1726	2.6230	6.8800	15.20
18. Tire & Rubber	.1709	1.5753	2.4816	9.22
19. Retail (Special Lines)	.1611	2.0913	4.3736	12.98
20. Chemical (Specialty)	.1596	1.9561	3.8264	12.26
21. Broadcasting/Cable TV	.1581	2.5167	6.3336	15.92
22. Finance	.1579	1.5786	2.4920	10.00
23. Trucking & Transport Leasing	.1484	2.5227	6.3640	17.00
24. Aerospace	.1478	1.6080	2.5856	10.88
25. Building	.1416	1.4873	2.2120	10.50
26. Auto Parts (Replacement)	.1405	1.7286	2.9880	12.30
27. Electronics	.1402	1.7944	3.2200	12.80
28. Precision Instruments	.1396	1.6888	2.8520	12.10
29. Auto Parts (Original Equipment)	.1345	1.6407	2.6920	12.20
30. Chemical (Basic)	.1339	1.8693	3.4944	13.96
31. Brewing	.1304	1.4009	1.9624	10.74

Table 4 (Continued)
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Industry	Coefficient of Variation ²	Standard Deviation ³	Variance ³	Average Rate of Return
32. Industrial Services	.1265	1.4190	2.0136	11.22
33. Retail Stores	.1152	1.3106	1.7176	11.38
34. Machine Tool	.1146	1.0796	1.1656	9.42
35. Packaging & Containers	.1028	1.2290	1.5104	11.96
36. Shoe	.1014	1.3951	1.9464	13.76
37. Railroad Equipment	.0971	1.1689	1.3664	12.04
38. Multiform	.0853	.8823	.7784	10.34
39. Drugstore	.0835	1.0800	1.1664	12.94
40. Newspaper	.0831	1.1798	1.3920	14.20
41. Publishing	.0713	.7605	.5784	10.66
42. Toiletries/Cosmetics	.0674	1.3008	1.6920	19.30
43. Food Processing	.0661	.8570	.7344	12.96
44. Soft Drink	.0635	1.2066	1.4560	19.00
45. NATURAL GAS PIPELINES ⁴	.0578	.7774	.6044	13.45
46. Fast Food	.0519	.9402	.8840	18.10
47. NATURAL GAS DISTRIBUTORS ⁴	.0479	.5224	.2729	10.90
48. Telecommunications	.0438	.4317	.1864	9.86
49. Drug (Proprietary)	.0326	.5953	.3544	18.26
50. Drug (Ethical)	.0272	.5122	.2624	18.84
51. Household Products	.0230	.3555	.1264	15.46
52. Health Care/Hospital Supplies	.0220	.3187	.1016	14.48

¹ Return on Net Worth is defined as: $\frac{\text{Net Income}}{\text{Common Equity and Preferred Stock}}$

² The coefficient of variation is a measure of relative variation of a series of data, i.e., a measure that expresses the size of the variation relative to the size of the quantity being measured. The coefficient expresses the degree of instability per percentage point of return.

³ The standard deviation expresses variation in terms of the distances (deviations) by which the various numbers depart from the mean. The variance is calculated by squaring the deviations and then averaging their squares. The square root of the variance is the standard deviation. Neither the standard deviation nor the variance provides information as to relative variability.

⁴ Gas industry data derived from A.G.A. Gas Facts, various issues.

Source: Value Line Investment Survey, various issues, except as noted.

TABLE 5
VARIABILITY IN RETURN ON NET WORTH¹
1977 - 1981
(Ranked by Coefficient of Variation)

Industry	Coefficient of Variation ²	Standard Deviation ³	Variance ³	Average Rate of Return
1. Sugar	.5865	5.5018	30.2696	9.38
2. Steel (Integrated)	.4920	3.2672	10.6744	6.64
3. Finance	.4287	3.6351	13.2136	8.48
4. Tire & Rubber	.3766	2.5382	6.4424	6.74
5. Textiles	.2948	2.2405	5.0200	7.60
6. Auto Parts (Original Equipment)	.2641	3.2641	10.6544	12.36
7. Steel (General)	.2508	2.9446	8.6704	11.74
8. Railroad Equipment	.1793	2.4523	6.0136	13.68
9. Paper and Forest Products	.1707	2.3048	5.3120	13.50
10. Building	.1669	2.2258	4.9542	13.34
11. Apparel	.1589	2.0527	4.2136	12.92
12. Broadcasting/Cable TV	.1535	2.6225	6.8776	17.08
13. Coal/Uranium/Geothermal	.1521	1.9590	3.8376	12.88
14. Home Appliances	.1437	1.9744	3.8984	13.74
15. Toys & School Supplies	.1384	2.1257	4.5184	13.36
16. Electronics	.1372	1.9835	3.9344	14.46
17. Machine Tool	.1366	2.1563	4.6496	15.78
18. Oilfield Services/Equipment	.1357	2.5858	6.6864	19.06
19. Metal Fabricating	.1351	2.0380	4.1536	15.08
20. Auto Parts (Replacement)	.1322	1.7348	3.0096	13.12
21. Trucking & Transport Leasing	.1229	2.0568	4.2304	16.74
22. Industrial Services	.1190	1.8271	3.3384	15.36
23. Advertising	.1118	2.2402	5.0184	20.04
24. Retail Stores	.1092	1.2859	1.6536	11.78
25. NATURAL GAS DISTRIBUTORS ⁴	.1000	1.2747	1.6248	12.75
26. Chemical (Specialty)	.0999	1.6020	2.5664	16.04
27. Multiform	.0979	1.2221	1.4936	12.48
28. Grocery Store	.0834	.9757	.9520	11.70
29. Brewing	.0813	.9541	.9104	11.74
30. Precision Instruments	.0810	1.2734	1.6216	15.72
31. Aerospace	.0775	1.2274	1.5064	15.84

Table 5 (Continued)
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<u>Industry</u>	<u>Coefficient of Variation</u> ²	<u>Standard Deviation</u> ³	<u>Variance</u> ³	<u>Average Rate of Return</u>
32. Medical Services	.0758	1.2706	1.6144	16.76
33. Health Care/Hospital Supplies	.0752	1.1662	1.3600	15.50
34. Chemical (Basic) ¹	.0737	.9786	.9576	13.28
35. NATURAL GAS PIPELINES ⁴	.0728	1.1320	1.2814	15.55
36. Retail (Special Lines)	.0540	.9912	.9824	18.36
37. Fast Food	.0488	.9287	.8624	19.04
38. Machinery	.0453	.6969	.4856	15.38
39. Drug (Proprietary)	.0447	.8333	.6944	18.64
40. Telecommunications	.0447	.5192	.2696	11.62
41. Toiletries/Cosmetics	.0443	.8424	.7096	19.02
42. Newspaper	.0437	.8035	.6456	18.33
43. Drug (Ethical)	.0422	.7985	.6376	18.92
44. Drugstore	.0417	.6794	.4616	16.28
45. Maritime	.0375	.6888	.4744	18.36
46. Packaging & Containers	.0335	.3655	.1336	10.92
47. Publishing	.0325	.5122	.2624	15.76
48. Electrical Equipment	.0270	.4707	.2216	17.42
49. Soft Drink	.0260	.5314	.2824	20.46
50. Household Products	.0233	.3795	.1440	16.30
51. Shoe	.0189	.3162	.1000	16.70
52. Food Processing	.0135	.1939	.0376	14.32

¹Return on Net Worth is defined as: $\frac{\text{Net Income}}{\text{Common Equity and Preferred Stock}}$

²The coefficient of variation is a measure of relative variation of a series of data, i.e., a measure that expresses the size of the variation relative to the size of the quantity being measured. The coefficient of variation expresses the degree of instability per percentage point of return.

³The standard deviation expresses variation in terms of the distances (deviations) by which the various numbers depart from the mean. The variance is calculated by squaring the deviations and then averaging their squares. The square root of the variance is the standard deviation. Neither the standard deviation nor the variance provides information as to relative variability.

⁴Gas industry data derived from A.G.A. Gas Facts, various issues.

Source: Value Line Investment Survey, various issues, except as noted.

TABLE 6
DEBT/EQUITY RATIOS¹
FOR
48 INDUSTRIES IN 1974²

1. Airlines	1.7	25. Agricultural Commodities	0.4
2. Telecommunications	1.1	26. Meatpackers	0.4
3. Electric Utilities	1.0	27. Aerospace & Defense	0.4
4. Financial Services	1.0	28. Vehicles (Autos & Trucks)	0.4
5. <u>NATURAL GAS DISTRIBUTORS</u>	<u>1.0</u>	29. Specialty Equipment	0.4
6. <u>NATURAL GAS PIPELINES</u>	<u>0.9</u>	30. Office Equipment Services	0.4
7. Contractors-Home Building	0.9	31. Electronics	0.4
8. Discount & Variety Stores	0.9	32. Chemicals	0.4
9. Entertainment	0.8	33. Nonferrous Metals	0.4
10. Lumber	0.8	34. Steel	0.4
11. Forest Products	0.6	35. Energy	0.4
12. Railroads	0.6	36. Banks	0.4
13. Packaging	0.5	37. Computers	0.3
14. Rail Equipment	0.5	38. Production Equipment	0.3
15. Tire & Rubber	0.5	39. Electrical Equipment	0.3
16. Housewares, Furnishings	0.5	40. Building Equipment	0.3
17. Supermarkets	0.5	41. Contractor-Heavy Construction	0.3
18. Department Stores	0.5	42. Appliances	0.3
19. Recreation	0.5	43. Beverages	0.3
20. Drug Chains	0.4	44. Toiletries & Cosmetics	0.3
21. Food Distributors	0.4	45. Publishing	0.3
22. Tobacco	0.4	46. Cement & Gypsum	0.2
23. Shoes	0.4	47. Drugs	0.1
24. Textiles	0.4	48. Insurance	0.0

¹Calculated by dividing long-term debt by the sum of stockholders' equity, minority stockholders' interest and accumulated deferred taxes and investment tax credits.

²The data for 1974 are as published in the January 1, 1975 issue of Forbes, except for gas industry data which were developed from A.G.A. Gas Facts.

TABLE 7
DEBT/EQUITY RATIOS¹
FOR
48 INDUSTRIES IN 1982²

1. Airlines	1.6	25. Packaging	0.4
2. Railroad Equipment	1.2	26. Steel	0.4
3. Financial Services	1.0	27. Building Equipment	0.4
4. Supermarkets	0.9	28. Housewares, Furnishings	0.4
5. Electric Utilities	0.9	29. Banks	0.3
6. Telecommunications	0.9	30. Chemicals	0.3
7. <u>NATURAL GAS DISTRIBUTORS</u> ³	0.8	31. Electronics	0.3
8. Contractors-Home Building	0.8	32. Computers	0.3
9. Discount & Variety Stores	0.8	33. Office Equipment/Services	0.3
10. <u>NATURAL GAS PIPELINES</u> ³	0.6	34. Production Equipment	0.3
11. Cement-& Gypsum	0.6	35. Specialty Equipment	0.3
12. Meatpackers	0.6	36. Contractors-Heavy Construction	0.3
13. Food Distributors	0.6	37. Vehicles (Autos & Trucks)	0.3
14. Department Stores	0.6	38. Aerospace & Defense	0.3
15. Drug Chains	0.6	39. Beverages	0.3
16. Energy	0.5	40. Tobacco	0.3
17. Forest Products	0.5	41. Recreation	0.3
18. Nonferrous Metals	0.5	42. Publishing	0.2
19. Lumber	0.5	43. Entertainment	0.2
20. Tire & Rubber	0.5	44. Toiletries & Cosmetics	0.2
21. Railroads	0.5	45. Shoes	0.2
22. Appliances	0.5	46. Drugs	0.2
23. Agricultural Commodities	0.4	47. Electrical Equipment	0.2
24. Textiles	0.4	48. Insurance	

¹ Calculated by dividing long-term debt by the sum of stockholder's equity, minority stockholders' interest and accumulated deferred taxes and investment tax credits.

² The data for 1982 are as provided in the January 3, 1983 issue of Forbes.

³ Gas industry data are for full year 1981, as provided in A.G.A. Gas Facts.

Source: Forbes, January 3, 1983, except as noted.

Mr. LUKEN. You said something about the advantages of a utility being open seven days a week. I don't know whether you said 24 hours, but you said 7 days a week.

Mr. ZEIGLER. Yes. We have people on call; yes, sir.

Mr. LUKEN. You were saying that in reference to offering service on the—

Mr. ZEIGLER. Consumer's premises.

Mr. LUKEN. For this diversified service?

Mr. ZEIGLER. No, sir. This would be in regard to calls from consumers. People move into homes over the weekend. They call us at night. They have pilot outages; they have emergency calls; they have suspected leaks.

Mr. LUKEN. Have they got problems with their water heater that you sold, or have they have got problems with their appliances that you sold? Have they got problems with the repair job that the utility furnished? You could provide that same service for that, couldn't you?

Mr. ZEIGLER. We provide that service, sir, for any gas appliances on our system. We sell a very small amount of appliances in our system.

Our utility sales are about \$260 million a year; our gas appliance and installation sales are less than \$5 million, or about 2 percent.

Mr. LUKEN. Well, you provide that service for any gas problem?

Mr. ZEIGLER. For any; yes, sir.

Mr. LUKEN. So you are not in the electric business?

Mr. ZEIGLER. No, sir; we are gas only. I should have said that to start with.

Mr. LUKEN. But some affiliates of the American Gas Association, they provide other kinds of diversified services and products?

Mr. ZEIGLER. Some companies have subsidiaries that—

Mr. LUKEN. Do they sell appliances that don't use gas?

Mr. ZEIGLER. That's right, sir. My company sells only gas appliances.

Mr. LUKEN. Well, they could provide the service then—24-hour service, 7 days a week.

Mr. ZEIGLER. None of them are available to do that, sir, in the smaller communities.

Mr. LUKEN. I'm speaking about all of them.

You know, we know that they are divergent. We have already established that. There is no universal characteristic to any of this—small communities, large communities, different kinds of utilities, gas utilities, electric utilities, gas and electric utilities, and different policies.

In my community, we don't have a utility that becomes involved in offering these services or selling any of these products. So I don't have any personal experience in it.

But it seemed to me, when you were mentioning the 7-day-a-week availability, that that of course is a great thing with reference to the regulated service, the providing of gas to the furnace and the hot water heater and service on that, like the telephone company does on their telephones and so on, but that when a utility gets into an unrelated business of remodeling or energy efficiency kind of renovation and so on, that they would also be able to

advertise, as the gentleman who preceded you showed, all these services in the name of the utility.

They could also provide the seven-day-a-week service, couldn't they?

Mr. ZEIGLER. Sir, I don't know how they are chartered, under their State charter, to operate. In our case, we are chartered to merchandise, to install, to sell the energy that is consumed in gas-burning appliances.

Mr. LUKEN. Only gas-burning appliances—only the energy?

Mr. ZEIGLER. No, I'm sorry. We are authorized to merchandise any type of appliance. We chose not to merchandise other than gas-burning appliances.

Mr. LUKEN. Do you merchandise kitchen stoves?

Mr. ZEIGLER. Yes, sir—gas stoves only, sir. And we probably supply—I'm guessing—approximately 10 percent of the market in our service area probably purchases gas appliances from the gas company. We do not sell any central systems, any central heating system; we do not sell boilers; we sell small, space-heating systems.

Yes, sir.

Mr. LUKEN. You say you sell 10 percent of the gas appliances.

Mr. ZEIGLER. That's an estimate on my part, sir.

Mr. LUKEN. OK. If a customer of yours buys the gas stove down at the appliance store and runs into a problem and calls you for service during the middle of the night, would that make a difference in any way as to whether that gas stove was purchased from you or from the appliance store?

Mr. ZEIGLER. No, sir.

Mr. LUKEN. Not at all?

Mr. ZEIGLER. Not at all.

Mr. LUKEN. You don't give any extra guarantee to that customer that if you sell it?

Mr. ZEIGLER. If it's within the 1-year product guarantee period, sir, we would have to supply a part.

Mr. LUKEN. If it's one from the appliance store, you are not going to take care of that—you are not going to back up that guarantee, are you?

Mr. ZEIGLER. We go out, and if the pilot is out, we will light the pilot.

Mr. LUKEN. No matter what is wrong with it, it is going to make a difference, isn't it?

Mr. ZEIGLER. If a part is needed and a part is supplied by us, we will install that part, and we will—

Mr. LUKEN. Twenty-four hours a day, 7 days a week?

Mr. ZEIGLER. We won't necessarily go out and put a—let's say they need a control on a gas stove, which is not a critical item. We might ask, "Could we come back in the morning and do the work?"

Mr. LUKEN. You might.

Mr. ZEIGLER. Not many people—

Mr. LUKEN. In reading your advertising I might believe, you are going to take care of it any time.

Mr. ZEIGLER. I don't think I—I didn't—what I said was, these emergency services we are available for certain things—burner adjustments, emergency calls, gas leaks—things that could be of a critical public safety nature to the consumer.

Mr. LUKEN. You don't do this through a subsidiary, do you?

Mr. ZEIGLER. No, sir. We have always—

Mr. LUKEN. Well, this is bound to get a little vague, isn't it, as to which operation you are working on? You send the same service people out?

Mr. ZEIGLER. When we sell—

Mr. LUKEN. Whether you sell it or somebody else sells it?

Mr. ZEIGLER. If we sell an appliance and we sell it on an installed basis, we mark that appliance up 1.70; we mark it up 70 percent. We add to that our estimated cost of installation. We make a profit on merchandise. We make a profit on the parts we supply, and we make a profit from the labor that we would charge if a part is required on a piece of equipment that we did not sell or a piece of equipment not in a warranty period.

We are not able to service all pieces of equipment, but in many cases we do have available, even for furnaces and heating equipment of this type, some universal controls that will allow people during the dead of winter to get back in business at any hour of the day, and we put a priority on heating-type problems that need to be serviced 24 hours a day.

If they call a heating dealer, he may be able to provide that same service, and, if so, fine. It is not done to do anything more than keep that person's home warm at a given time when he might not be able to get service, and I think most utilities provide a similar type service.

Mr. LUKEN. Do you sell furnaces, too?

Mr. ZEIGLER. No, sir.

Mr. LUKEN. You don't sell furnaces?

Mr. ZEIGLER. No, sir.

We sell space heaters—the small circulator-type heaters that will heat a given small space, a single room or possibly two rooms.

Mr. LUKEN. Getting back to the stove, you send the same people out, whether it is a stove you sell—what brand stove do you sell?

Mr. ZEIGLER. Hardwick, Roper, Magic Chef.

Sir?

Mr. LUKEN. You sell more than one manufacturer?

Mr. ZEIGLER. Yes, sir.

Mr. LUKEN. But you send the same service person out, if there is a service call on that gas stove—whether it is one that you sold or whether it is one that the appliance store sold?

Mr. ZEIGLER. It could be the same person, particularly in the smaller communities where we have a man doing more than one job. If it's a larger community, we have people available for service work only. We have also some people—

Mr. LUKEN. But when that man gets there, depending upon the nature of the problem, he can do more if it is from your store than if it was obtained from the appliance store—right?

Mr. ZEIGLER. He may or may not be able to. He may have to order a part from—

Mr. LUKEN. Well, that would be reassuring to me. That might be an inducement to me to buy the stove from you.

Mr. ZEIGLER. Yes, sir, I agree.

Mr. LUKEN. Even though it was the same price.

Mr. ZEIGLER. Yes, sir.

Mr. LUKEN. Thank you.
Yes, sir?

TESTIMONY OF THOMAS D. MORRON, VICE PRESIDENT, CUSTOMER SERVICES AND MARKETING, EDISON ELECTRIC INSTITUTE

Mr. MORRON. Mr. Chairman, my name is Tom Morron. I'm here representing the Edison Electric Institute, which is the association representing the Nation's investor-owned electric utilities.

Our members serve 98 percent of the customers reached by this segment of the utility industry, and we generate 78 percent of all the electricity used in the United States, providing service to more than 76 percent of all of the electric utility customers in the Nation.

As you know, Mr. Chairman, from a perusal of my prefiled testimony, the focus of EEI's position is on the availability of redress to parties who may feel that an anticompetitive marketing practice is in force, and I would like to summarize that testimony briefly.

Depending on local circumstances, some electric utilities actively market energy conservation or load management, while others market new uses of electricity to improve the utilization of existing generation capacity.

These marketing programs take many forms, including the promotion of energy-efficient appliances through rebates or, in some cases, direct supply, the conduct of energy audits for residential and commercial buildings, supply of or financing for weatherization materials, dissemination of conservation information, financing of customer-initiated activities, implementation of rate options, and the provision for direct load control of water heaters and other appliances for peak load reduction.

In some of these programs, the utility may be involved in activities that affect a local contractor's market.

Utility participation in marketing activities that incorporate customer needs and utility goals provides, we think, many benefits to the ratepayers and to society as a whole.

First, utility participation is likely to foster competitive markets for new products and services by increasing overall demand for the products or services. Many small business contractors can share in the benefits of these new markets.

Second, overall utility efficiency can be improved, resulting in lower rates.

Finally, utilities can bring to this competitive marketplace expertise in electricity end use, which will help to ensure efficient use of the Nation's resources.

Overall, we believe that utility marketing activities, given regulatory protections which are already in place, provide a strong benefit to the Nation's utility customers.

In all cases, the local regulatory body, the public utility commission, or PUC, as it is called—has sufficient authority to assure that such utility activities are not improperly cross-subsidized.

State regulators maintain authority to review all utility transactions to determine which expenses a utility should properly recover in its rates, including expenses related to marketing activities.

State regulators also have the authority to review all transactions between a regulated utility and its affiliates or subsidiaries and the allocation of costs between a utility and nonutility business enterprise to ensure that improper cross-subsidization does not occur.

Existing antitrust and unfair trade practice laws also provide protection to small businesses. If a utility enters a competitive market, it is subject to all of the applicable State and Federal laws restricting unfair trade practices and abuse of monopoly power.

Thus, any attempts by utilities to compete unfairly in competitive markets based on their monopoly position in a regulated business can and should be subjected to close legal and regulatory scrutinies before PUC's, agencies responsible for enforcing antitrust and unfair trade practice laws, as well as our court system.

On a national level, EEI has worked with the Office of Advocacy at the Small Business Administration to address the concerns and interests of small business. Unfortunately, the recommendations presented by the Office of Advocacy, in its document entitled "Competition Recommendations Concerning Utility Energy Programs and CACS Plan," are based, in our judgment, on unsupported and erroneous premises and fail to fully take into account Federal energy conservation goals and are so restrictive as to be, in themselves, anticompetitive.

We have attached for your information, Mr. Chairman, and the information of the committee an in-depth critique of this document for your perusal.

Mr. Chairman, no utility company develops its marketing program in a vacuum. Questions concerning competition issues and internal or cross-subsidization of competitive activities are analyzed by electric utilities from the very beginning of the marketing planning process.

In addition, Federal mandatory programs such as the residential conservation service and the commercial and apartment conservation service, and voluntary programs, like the residential energy efficiency program, include specific criteria to maintain adequate competition and place the cost allocation issue appropriately at the State regulatory level.

States may develop programs of their own that mandate utility involvement in competitive activities. However, these programs are developed specifically for the energy characteristics of the State, and the State regulatory body assumes the responsibility to analyze anticompetitive concerns of small businesses which might arise thereby.

If a small business has a specific concern with a utility company's marketing processes or practices, the Edison Electric Institute urges that business to try to reach a resolution directly with that utility.

If there is no other recourse, the appropriate State or local governmental agency can be approached; and, moreover, as indicated previously, we are convinced that there are sufficient legal regulatory mechanisms already in place to prevent unfair practices.

Adding additional regulatory burdens, in our belief, will only increase utility difficulty in promoting cost-effective programs which will, in the long term, benefit both the utility and its ratepayers.

Thank you, Mr. Chairman, for this opportunity to present our views on the matter, and I would be pleased to answer any questions you might have.

[Mr. Morron's prepared statement with attachment follows:]

PREPARED STATEMENT OF THOMAS D. MORRON, VICE PRESIDENT, CUSTOMER SERVICES
AND MARKETING, EDISON ELECTRIC INSTITUTE

Good morning, Mr. Chairman and members of the Subcommittee on Antitrust and Restraint of Trade Activities Affecting Small Business. My name is Tom Morron. I am Vice President of the Customer Services and Marketing Division of the Edison Electric Institute (EEI).

The Edison Electric Institute is the association representing the nation's investor-owned electric utilities. EEI members serve 98 percent of the customers reached by this segment of the electric utility industry. They generate 78 percent of all the electricity in the United States and provide service to more than 76 percent of all electric utility customers in the nation.

As the costs associated with the generation, transmission and distribution of electricity have escalated, electric utilities have organized marketing programs, including energy conservation and load management programs, and supply and installation programs for the purpose of reducing the use of critical fuels, minimizing the need for costly new generating facilities, and helping ratepayers manage the size of energy bills. These programs have resulted in the modification of kilowatt hour consumption patterns and kilowatt demand profiles, saving billions of dollars. With this background of experience, we are pleased to be afforded the opportunity to comment on activities such as supply, installation, service of heating and cooling systems and other marketing practices in the electric utility industry.

"Marketing" in the electric utility industry is a word that is subject to many interpretations. In my statement today, marketing encompasses any demand-side strategies that bring the needs and wants of the consumer into better equilibrium with the industry's capability to produce electricity to the benefit of all involved. Demand-side programs encompass utility-initiated activities designed both to help customers achieve their goals of reducing costs and conserving energy while simultaneously maintaining lifestyles, and to achieve utilities' goals of influencing the utility load shape in such a way as to improve financial performance, reduce capital requirements and increase system utilization.

Demand-side alternatives, and in particular, options that give residential customers greater control over their electricity usage and their total energy bill, provide to the customer a positive signal that the utility is concerned about high electric bills and is providing the means to control future expenditures for energy. Electric utility programs falling under this definition include: load management (peak shaving, valley filling and load shifting), shaping load through new uses, strategic conservation, and industrial electrification.

In discussing utility marketing practices, it is important to recognize that differences in system and customer characteristics cause utility marketing practices to vary among individual companies. As a result of these system-specific differences, it is difficult to provide generalized statements about "national" marketing practices.

Depending on local circumstances, some electric utilities actively market energy conservation or load management while others market new uses of electricity to improve the utilization of existing capacity. These marketing programs take many forms, including the promotion of energy-efficient appliances through rebates or direct supply, the conduct of energy audits for residential and commercial buildings, the supply of or financing for weatherization materials, the dissemination of conservation information, the financing of customer initiated activities, the implementation of rate options and the provision for direct load control of water heaters and other appliances for peak load reduction. In some of these programs the utility may be involved in activities that affect the local contractors' market.

Utility participation in marketing activities that incorporate customer needs and utility goals provides many benefits to ratepayers and society. First, utility participation is likely to foster competitive markets for new products and services by increasing overall demand for the products or services. Many small business contractors can share the benefits of these new markets. Second, overall utility efficiency can be improved, resulting in lower rates. Finally, utilities can bring to this competitive marketplace expertise in electricity end-use which will help to ensure efficient use of resources. Overall, we believe that utility marketing activities, given regulatory protections which are already in place, provide a strong benefit to the customer.

In all cases, the local regulatory body (public utility commission or PUC) has sufficient authority to assure that such utility activities are not improperly cross-subsidized. State regulators maintain authority to review all utility transactions to determine which expenses a utility should properly recover in its rates, including expenses related to marketing activities. State regulators also have the authority to review all transaction between a regulated utility and its affiliates, and the allocation of costs between a utility and non-utility business to assure that improper cross-subsidization does not occur.

Existing antitrust and unfair trade practice laws also provide protection to small businesses. If a utility enters competitive markets, it is subject to all state and federal laws restricting unfair trade practices and abuse of monopoly power. Thus, any attempts by utilities to compete unfairly in competitive markets based on their monopoly position in a regulated business can be subjected to close legal and regulatory scrutiny before PUC's, agencies responsible for enforcing anti-trust and unfair trade practice laws, and the courts.

It is important to note that the electric utility industry has been attempting to work closely with small business groups on many levels. At the local level, a number of electric utility and contractor groups have established organizations to improve relations. For example, in Kansas, Delaware and Missouri, heat pump associations consisting of representatives of manufacturers, distributors, installers and contractors have been established to

promote the use of electric heat pumps. The utilities involved anticipate that increasing the heat pump share of the space heating market will improve the utilities' load characteristics. Moreover, manufacturers, distributors, installers and contractors all stand to benefit from increased sales.

In Pennsylvania, California and Arizona electric leagues have been established where electrical contractors and the electric utilities discuss matters of interest in an open forum.

Organizations such as heat pump associations and electric leagues speak for utilities and interested small businesses in their territories and have contributed to some of the most successful marketing and consumer education programs in the nation. This team approach has been used to initiate consumer action affecting all parts of the energy conservation industry and is responsible for many successful results. In the Philadelphia area for example, the coalition of electric contractors and the local utility has provided information resulting in the installation of 3,163 heat pumps. These approaches create forums which can assist small business in responding to changing market conditions, and provide a mechanism for communicating these changes and modifying the participants' future approach to the market. The net result is that the utility and interested small businesses continue to work together for their mutual benefit.

On a national level, EEI has worked with the Office of Advocacy at the Small Business Administration to address the concerns and interests of small businesses. Unfortunately, the recommendations presented by the Office of Advocacy in "Competition Recommendations Concerning Utility Energy Programs

and CACS Plan" are based upon unsupported and erroneous premises, fail to fully take into account Federal energy conservation goals and are so restrictive as to be anti-competitive. We have attached, for your information, an in-depth critique of the Office of Advocacy recommendations.

No utility develops its marketing program in a vacuum. Questions concerning competition issues and internal or cross-subsidization of competitive activities are analyzed by most electric utilities from the beginning of the marketing planning process. In addition, Federal mandatory programs such as the Residential Conservation Service, and the Commercial and Apartment Conservation Service and voluntary programs like the Residential Energy Efficiency Program, include specific criteria to maintain adequate competition and place the cost allocation issue appropriately at the state regulatory level. States may develop programs that mandate utility involvement in competitive activities. However, these programs are developed specifically for the energy characteristics of the state and the state regulatory body assumes the responsibility to analyze anti-competitive concerns of small businesses which might arise.

If a small business has a specific concern with a utility company's marketing practices, EEI urges that the business try to reach a resolution directly with the utility. If there is no other recourse, the appropriate state or local governmental agency can be approached. Moreover, as indicated previously, we are convinced that there are sufficient legal regulatory mechanisms already in place to prevent unfair practices. Adding additional regulatory burdens, in our belief, will only increase utility difficulty in promoting cost-effective programs which will in the long term benefit both utilities and ratepayers.

Thank you for this opportunity to present EEI's views on this matter.

EEl CRITIQUE OF THE SMALL BUSINESS ADMINISTRATION
OFFICE OF ADVOCACY REPORT ON UTILITY COMPETITION
WITH SMALL BUSINESS

The Office of Advocacy of the Small Business Administration has recently published a report entitled "Utility Competition with Small Businesses: Recommendations for States on Utility Energy-Related Programs and the Commercial and Apartment Conservation Service Program" (March 1984). The Office of Advocacy consulted with the Edison Electric Institute (EEI) during the preparation of this report. While the Office of Advocacy implemented a few of the suggestions offered by EEI, particularly those which corrected minor factual errors, EEI and the Office of Advocacy continue to disagree with respect to the underlying premises of the Office of Advocacy recommendations as well as with the specific recommendations offered. This paper is intended to identify those areas of continuing disagreement.

EEI believes that the fundamental premises of the Office of Advocacy are inaccurate. In particular, the Office of Advocacy errs in the following areas:

1. The Office of Advocacy incorrectly assumes that utility competition is inappropriate. The background paper assumes that utilities are somehow different from the "private sector" and that utility (or utility affiliate) competition with small business is implicitly unfair. We disagree. Utilities are an important and

vital element of the private sector. As such they should have the opportunity to compete equally with other businesses. For example, the recent divestiture agreement for the AT&T system now permits various operating companies to engage in competitive, non-utility business. Utility (or utility affiliate) competition can benefit consumers by providing increased options, more competition, increased convenience and/or lower prices. Proposals to preclude such utility (or utility affiliate) competition with other segments of the private sector are actually anti-competitive in nature and contrary to the intent and requirements of our anti-trust laws.

Existing laws and regulations provide significant protections against and remedies for unfair competition. The Office of Advocacy has not shown that these mechanisms fail to work adequately. Moreover, utilities engaging in non-utility business activities are monitored by public utility commissions and intervenors to assure that utility ratepayers are not improperly subsidizing such businesses. This form of review is more appropriate than and far preferable to the explicit ban on non-utility businesses which the Office of Advocacy proposes.

The Office of Advocacy has disregarded the Congressional policy goals implicit in imposing RCS and CACS program obligations on utilities. Utility conduct of the RCS and CACS programs, including provision of audits, is mandated by the provisions of the National Energy Conservation Policy Act (NECPA), as amended by

the Energy Security Act (ESA). In enacting these laws, Congress determined that utilities are appropriate entities to promote the adoption of energy conservation measures by utility customers. The Office of Advocacy fails to take into account the extent to which utilities further these goals.

3. There is no need for recommendations of such a drastic and intrusive nature. The Office of Advocacy concedes that few, if any, utilities (or utility affiliates) offer supply and installation services for the buildings covered by the CACS program. Since utilities rarely compete in this area, the possibility for unfair competition with small businesses appears insignificant. Moreover, the Office of Advocacy fails to show that electric utilities (or utility affiliate) have been found to compete unfairly with small businesses. Under these circumstances, there appears to be no basis for the stringent prohibitions and restrictions which the Office of Advocacy proposes.

In addition to these core concerns, we have the following specific objections to the recommendations presented by the Office of Advocacy.

1. Utility Energy Programs (General Recommendations)

The recommendation that utility supply and installation programs be prohibited is unwarranted, particularly with respect to the CACS program. While Congress prohibited many utility

supply and installation programs for RCS customers (Section 216 of NECPA, 42 U.S.C. 8216), it imposed no such prohibition for CACS services. The DOE CACS rules properly recognize that utility activities relating to supply, installation and financing may be permitted, subject to public scrutiny, during development of the State Plan. DOE also recognizes that the rate hearing process affords an additional opportunity for scrutiny. Moreover, DOE requires that if a State Plan permits an auditor to recommend a supplier, contractor, or lender, the State plan must contain procedures to prevent unfair discrimination. 48 F.R. 49629. Such procedures can be far less intrusive than completely prohibiting utility participation in these areas.

The recommendation limiting utility conservation programs to financing/voucher programs is unnecessarily restrictive. Utilities have developed a wide range of energy conservation programs in order to manage the need for incremental utility facilities, inform consumers of available energy conservation opportunities and promote energy efficiency and the use of energy conservation measures. While financing/voucher programs are one method for achieving these goals, other approaches to address their specific needs and circumstances may be more cost effective for the utility and its customers.

The relative benefits of various types of utility programs could be addressed in a hearing on State Plans for the CACS program. Moreover, as shown by the testimony of Timothy Muris

before the Senate Small Business Committee on November 2, 1983, utility participation in conservation activities may benefit consumers by increasing consumer convenience and reducing the costs of finding valuable services. Financing programs may actually be pro-competitive by increasing the market for a variety of conservation-oriented goods and services. A flat restriction, as the Office of Advocacy proposes, would be anti-competitive, for it could deprive utilities and consumers of the opportunity to benefit from programs which may be more efficient to the utility and more advantageous to the consumer.

The recommendation for a public hearing regarding supply and installation programs simply repeats an existing DOE requirement. Section 458.303 of the DOE CACS regulations imposes the requirement for notice, comment and a public hearing on a State Plan. This would provide a forum for discussing whether utility supply and installation programs should be permitted in a state CACS program.

Energy related service programs, such as maintenance and repair, should not be prohibited. Virtually all utilities are required to provide their service under "safe, adequate and reliable" conditions. Maintenance and service programs can play an important role in achieving these important utility obligations. Moreover, effective maintenance and service (such as furnace upkeep) can prevent improper waste of energy resources

and thereby promote national and utility energy conservation goals.

II. Utility Supply and Installation Programs.

The recommendation that utilities should be required to demonstrate substantial public benefits before they may engage in supply and installation programs imposes a burden on utilities not shared by other potential entrants in that business. This burden to entry has serious anti-competitive implications. EEI submits that such a burden is not warranted in the absence of significant evidence that utility supply and installation programs are themselves anti-competitive. Since the the Office of Advocacy concedes that there are few such programs and has not identified specific programs as being anti-competitive, there is no basis for recommending such intrusive pre-approval requirements.

The recommendation that utility supply and installation activities should be conducted only in a separate subsidiary is unnecessary to avoid cross-subsidization. The provisions of 42 U.S.C. 8283(b)(1) require that costs and revenues for activities attributable to utility CACS programs be "accounted for on the books and records of the public utility separately from amounts attributable to all other activities of such utility." Supply and installation activities conducted as part of the CACS program would be covered by this requirement, thereby providing the data that the Office of Advocacy seeks. Moreover, public utility

commissions generally have access to all utility books to assure there is no improper cross-subsidization.

III. Energy Audits.

The suggestion in the background paper that utilities may unfairly compete with private energy auditors by subsidizing audits fails to take into account the national energy policy goals of NECPA and the ESA. The decision whether to subsidize a utility audit is made by each state after balancing energy conservation goals, ratemaking policies, competitive factors and other considerations. The Office of Advocacy has not explained how its recommendations affect the achievement of energy policy goals.

The recommendation that a utility "contract out" energy audits ignores the fact that Congress specifically imposed the audit obligation on utilities. NECPA authorizes, but does not mandate, utilities to contract out their audit responsibilities, and specifically permits contracting out to other utilities. 42 U.S.C. 8283(a). Some utilities may contract out audits to small businesses if they determine this is a cost-effective approach. However, if a utility has the required expertise, using utility personnel may be more cost-effective and thus the more reasonable approach. The choice of approach requires a particularized analysis for each utility's operation, not a rigid rule.

IV. Supply and Installation Recommendations by Energy Auditors.

The Office of Advocacy recommendation that "energy audit recommendations should be limited to the DOE minimum requirements of providing general advice" may not be adequate to achieve state energy conservation goals. Congress provided detailed guidelines about the type of information and degree of specificity required of utility energy audits.

The Office of Advocacy's concerns about recommendations to prohibit discussion of fuel-switching appears to ignore several important considerations. First, the definitions of program measures in Section 458.104 of the DOE CACS regulations expressly prohibit auditors from recommending fuel-switching unless specifically authorized by the State Plan pursuant to Section 458.305(d) (4) of the DOE regulations. The State Plan may permit such recommendations if this furthers a state's particular energy conservation needs. Assuming fuel-switching recommendations are permitted, it is important to remember that fuel-switching generally involves an expensive investment. Eligible customers covered by the CACS program are not likely to undertake such an investment without seeking advice from several advisors, which are likely to include small business.

While it may be useful to advise consumers about alternative sources of information, requirements for specific statements about

"potential conflict of interest" are inappropriate because they (1) imply improper action, which has not been found, (2) are excessively paternalistic, and (3) impose unfair competitive burdens. We see no reason why a utility auditor would be in any different situation than a Covered Building Heating Supplier auditor (which may represent a small business). Since the Office of Advocacy does not propose "conflict of interest" disclosure requirements for small business auditors, there is no reason to treat utility auditors differently.

V. Availability of Audit Results.

The Office of Advocacy recommendation restricting utility use of audit results ignores the fact that few utilities provide supply and installation services to customers covered by the CACS program. Under these circumstances, there seems to be little reason for these recommendations. Moreover, the Office of Advocacy ignores the fact that 42 U.S.C. 8283 (a)(3) requires utilities to retain audit results for ten years and to provide such information to subsequent customers. The the Office of Advocacy also cites no legislative history which suggests Congress intended to restrict internal utility audit record-keeping.

VI. Expansion of Measures and Equipment or Buildings.

This recommendation repeats requirements of the DOE CACS program regulations and is thus unnecessary.

For the foregoing reasons, EEI respectfully suggests that the Office of Advocacy recommendations are based on faulty premises, are far too restrictive, and are actually anti-competitive in nature.

Mr. LUKEN. I'd just like to take one aspect of your testimony. You say, "For example, the recent diversification agreement for the AT&T system now permits various operating companies to engage in competitive non-utility business." Haven't you oversimplified that just a little bit?

Mr. MORRON. I suspect so, Mr. Chairman.

Mr. LUKEN. Doesn't Judge Greene put a few qualifications on that ability? One of them would be not to use the Bell logo; isn't that right?

Mr. MORRON. Yes, sir.

Mr. LUKEN. But these gentlemen who testified today pointed out that one of the main points of their criticism was that here we have a regulated monopoly like the Indiana Gas or the Washington Gas, which has built up a reputation, stability, confidence in the name, and uses that name in order to sell these products.

You can't do that—AT&T can't do that.

Mr. MORRON. I understand, Mr. Chairman.

Mr. LUKEN. But Indiana Gas isn't, and Washington Gas isn't.

Mr. MORRON. Mr. Chairman, with respect to the earlier comments about AT&T diversification and somewhat to your point here, I would also point out that cross-subsidization was a regulatory policy decision in that industry prior to its diversification, and utility regulators at the State level and at the Federal level were perfectly able to determine whether or not a cross-subsidization was taking place between local service, long distance lines, and so on, and between remote switching stations and urban switching stations, and so forth.

The point that we seek to make here is that same body that is able to make such determinations over a number of years in the phone company case and make such cross-subsidization determinations every day in electric utility cases as well as gas are perfectly capable of answering the questions that are raised by the small business representatives here today.

Mr. LUKEN. I submit that that is not what I get out of your statement. I'm just talking about your statement and just one aspect of it, and I'm not prepared to deal with the entire statement, but what you say is, "As such, they should have the opportunity—the utilities, the monopolies—to compete equally with other business," and the first example you use, "For example, the recent diversification agreement for the AT&T now permits various operating companies to engage in competitive nonutility business."

I suggest, and especially in view of your not agreeing—I suggest that that statement is inappropriate, and it's just wrong, as an example of what you are trying to say here, because, as a practical matter, we have had that industry, the telephone industry—under Ma Bell operating for many, many years, but operating under a consent agreement with regard to unregulated services.

They have been under a consent agreement for many, many years, that, when they were not permitted to offer these unregulated services.

That has been the order of the day with them, as contrasted with your industry. You have not had those regulations offering these services.

So when they got around to being permitted to offer other services, first they had to go through Judge Greene, they can't use the logo, and I think there are quite a few other restrictions, and they can't even use the same name; they first had to be divested into different companies.

There are other restrictions that just don't apply to your situation.

So what I am saying is that this comparison doesn't lie.

Mr. MORRON. I'm sorry you feel that way, Mr. Chairman.

Mr. LUKEN. Well, I have said why. If you want to address what I have said, of course you may.

Mr. MORRON. I portray no expertise in the telephonic communications regulatory—

Mr. LUKEN. Oh, I don't either, but I've been exposed to a bit of it.

Mr. MORRON. But, Mr. Chairman, I would say that the point to be made here is that if there is improper cross-subsidization taking place with a nonutility enterprise in competition with a small businessman, the local commission is perfectly capable of making a judgment as to whether there is cross-subsidization—

Mr. LUKEN. The local commission? You mean the State commission?

Mr. MORRON. Yes, sir. I've testified before a number of them prior to joining EEI, and I can tell you that every rate case that is prosecuted includes at the State level an assessment of subsidization.

In the case of any of the rate cases, they are normally divided into two—

Mr. LUKEN. I'm inclined to argue with that one pretty strongly, too.

Mr. MORRON. Well, if you would allow me to finish—

Mr. LUKEN. I have not been in those cases, but it is my clear impression, as the people who have testified before you testified, that the mission—the injunction to the public utility commission is not to enforce the antitrust laws, not to protect the contractors out there—the small-business people—with regard to their protection of antitrust laws or discrimination, but simply to consider cross-subsidization with a view to the ratepayer.

We are not talking here about the ratepayer. That may be a consideration. But the public utility commission is only interested in the ratepayer, as far as I know.

Mr. MORRON. Mr. Chairman, small businessmen are ratepayers as well, and so they fall into—

Mr. LUKEN. I think you are really trying to confuse this situation.

Mr. MORRON. No, sir, I'm not.

Mr. LUKEN. Of course they are ratepayers, but we are not talking about their role as ratepayers now; we are talking about their role in providing a service and a product.

Mr. MORRON. And, Mr. Chairman, what I am suggesting to you is that the State regulatory commission, if cross-subsidization is of such great concern to a small businessman who feels that he is being unfairly competitive—competed against by a utility, and by reason of the utility's success or the reason for, rather, the utility's success is that the utility has financial strength derived from its

utility operations that it then applies to its nonutility operation, the local commission—the State regulatory commission is perfectly capable of ascertaining whether (a) cross-subsidization is in fact taking place; and (b) whether, in their judgment, that cross-subsidization is in the best interests of the ratepayer.

Mr. LUKEN. Do you know of any case where the utility commission seriously considered such a case with reference to these issues?

Mr. MORRON. I have no personal knowledge of it, but I can tell you——

Mr. LUKEN. I didn't need to go so far as to say did you ever know of a case where the public utility commission actually ruled against a utility but I'm asking you if they have ever even considered such an issue.

Mr. MORRON. I was involved in a case with my previous employer, Arizona Public Service Co. in Phoenix, AZ, before the Arizona Corporation Commission, the body having jurisdiction over our rates, where the question of a marketing program having to do with a waste-heat-recovery water heater was——

Mr. LUKEN. Of a what?

Mr. MORRON. A waste-heat-recovery water heater. It is a device that takes the waste heat discharged by an air-conditioner and heats your water with it, which Arizona Public Service Co. was actively marketing at that point as the State's only distributor of it.

A question was raised as part of that proceeding whether this was anticompetitive. I cannot, in good conscience, tell you, Mr. Chairman, that there was an exhaustive investigation. It was quickly determined that nobody else in the State wanted to take the device on that we did.

That is my only personal knowledge of a commission investigating an anticompetitive charge. Such a charge was made and was rejected.

Mr. LUKEN. Well, suffice it to say that your testimony on this point is not necessarily persuasive on the issue, and I do challenge the reference here as to the AT&T system diversification being any basis for the arguments that you maintain for a regulated monopoly getting into these other services and the furnishing of other products.

I think the reverse is true and based upon our experience with the telephone companies, that if, for example, this was a universal practice, I think Congress would have dealt with it, or the courts would have dealt with it, as it dealt with AT&T and would have put in protections for the competition when dealing with one entity, whether through a direct subsidiary or without any subsidiary, one entity being the regulated and the nonregulated business.

I think protections would have been built in, and that's what is being requested here.

I'm of the impression that, since there isn't any universal practice, and since we are dealing with small and large utilities across the country of very dissimilar kinds of operations, that it is hard for the Federal Government really to get a handle on it. It's hard for Congress to really get a handle on it. Whether we can or not I don't know.

Evidently, one of the reasons we have gotten into it is the emergency of the energy audit under the Federal legislation, and this may be a handle, but as has been discussed, we have passed some legislation in the RCS program and we may pass some in CACS as it develops.

I have no further questions. Is there anything either one of you wants to offer further?

Mr. MORRISON. I think perhaps I have said enough.

Mr. ZEIGLER. Mr. Chairman?

Mr. LUKEN. Surely.

Mr. ZEIGLER. I'd like to make one more comment.

Mr. LUKEN. You may have the last word.

Mr. ZEIGLER. All right. I didn't want to leave the impression that we don't solicit and need the support of all of our contractors and dealers—small business operators in the energy-related field. We couldn't live in the gas industry without their assistance and help, and we do spend a good bit of our time and effort, I think, productively, on their behalf in working with their representatives, turning prospects over to them, talking to customers about what they can expect to get from gas, trying to educate the public as to what new appliances—higher tech appliances, more efficient appliances—are available.

We need their help and support, and, frankly, I think we are getting a little bit of a bad rap overall on the fact that we may compete in some small areas.

Mr. LUKEN. Your company or your association?

Mr. ZEIGLER. The association, sir.

Mr. LUKEN. You are talking about some of your companies in the association?

Mr. ZEIGLER. Yes, sir.

Mr. LUKEN. Well, that could be. I'm sure that you do, and that most utilities do exactly what you say, and it's not my intention and has not been my intention to convey any other meaning.

I'm trying to raise questions on a hypothetical basis. None of it is intended, certainly, to be a criticism of any individual or any company.

Mr. ZEIGLER. I understand, sir. I didn't mean it that way.

Mr. LUKEN. OK. Well, thank you very much, gentlemen. We appreciate it.

Charles Gray, assistant general counsel, National Association of Regulatory Utility Commissioners.

Maybe Mr. Gray can shed some light on this question, but first we have your testimony, I believe, and it will be received in the record, and you may proceed.

**TESTIMONY OF CHARLES GRAY, ASSISTANT GENERAL COUNSEL,
NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS,
ACCOMPANIED BY LINDA KENT, DIRECTOR OF CONGRESSIONAL RELATIONS**

Mr. GRAY. For the record, my name is Charles Gray. I am assistant general counsel of the National Association of Regulatory Utility Commissioners. I'm accompanied today by Linda Kent, our director of congressional affairs.

Our association, of course, represents the State public utility commissions, whose names have been thrown around fairly vigorously today.

I will briefly summarize our statement. I think it is important to make the sort of paramount point that our members' primary concern, if not exclusive concern, in these issues is the protection of ratepayer interests, broadly defined, and specifically in the area of diversification of utilities into non-regulated areas.

Again, the priority is the protection of ratepayers, and what that means is the elimination or control of cross-subsidies that take money from ratepayers for nonregulated competitive enterprises.

The primary means that our members use are accounting procedures, in order to ensure that the right dollars go in the right accounts and that the ratepayers are not providing funds for competitive activities, oversight of diversification, either through prior approval of diversification, into nonregulated areas, as well as limitations on the scope and nature of diversification.

Again, these are for the protection of ratepayers in the interests of not allowing the utility to put too many eggs in a competitive basket, where it may fail.

On the question of whether or not a State commission is a good forum if a small business competitor is having a problem with the utility, it seems to me that the commissions can provide a forum. I'm not convinced it's the exclusive forum or perhaps even the best forum for these kinds of complaints.

It seems to me that the small businessman is most likely to get the attention of a State regulatory body and obtain some remedy for his complaints if he can allege and prove that not only is the utility hurting his business but also hurting the ratepayers through the activities that he complains of.

It is less likely, it seems to me, if he has got what I consider more of a pure antitrust complaint in which the subsidies are hard to find, that the small business competitor comes in and says, "By the sheer size of this utility, by its context in the community, I can't compete," and without the ability to show specific anticompetitive problems, where the dollars are misallocated, I think the commissions, for a number of reasons, are less likely to provide the kind of relief the competitor wants.

I think there are practical reasons for that—legal and practical perhaps.

First of all, not every commission is going to have jurisdiction over these kinds of antitrust complaints, and it is true at the Federal level as well as the State level.

FERC, for example, had to have price squeeze jurisdiction forced on them by the courts. They didn't go looking for that kind of more or less antitrust approach.

Also, it is a question of State resources. Some commissions are small; some are large. Some have extensive staffs; some have smaller staffs.

It is also a question of scheduling. As you may know, right now, the State commissions are dealing with the breakup of the Bell System, the first threatened bankruptcy of electric utilities that is being bandied all over the newspapers. They are dealing with deregulation of natural gas in less than a year.

So in a lot of ways, the priority that I started out with here—the protection of ratepayers—is going to require that they devote their attention to these broader issues, and if I also may add, in many cases the commissions are having to deal with and sort out problems that were created at the Federal level.

I point out that in all three of these areas, the three major utilities—telephone, gas, and electric—the commissions have found that protecting ratepayers has become a more difficult task in the last 4 or 5 years.

That completes my summary, and I would be happy to answer any questions you may have.

[Mr. Gray's prepared statement with attachment follows:]

PREPARED STATEMENT OF CHARLES GRAY, ASSISTANT GENERAL COUNSEL, NATIONAL
ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS

Good afternoon, Mr. Chairman and Members of the Committee:

My name is Charles Gray. I am Assistant General Counsel of the National Association of Regulatory Utility Commissioners, commonly referred to as the NARUC, on whose behalf I am testifying today. Accompanying me today is Linda Kent, NARUC Director of Congressional Relations.

The NARUC is a quasi-governmental, nonprofit organization founded in 1889. Within our membership are the governmental agencies of the fifty States, the District of Columbia, Puerto Rico and the Virgin Islands which are engaged in the regulation of utilities and carriers. Our chief objective is to serve the consumer interest by seeking to improve the quality and effectiveness of government regulation in America.

The members of the NARUC appreciate this opportunity to participate in the Subcommittee's investigation of the competitive activities of regulated utilities as they affect small businesses. As the national representative of the State regulatory commissions, the NARUC has taken an active interest in utility diversification into non-regulated businesses, and in fact, in August 1981, established our Ad Hoc Committee on Utility Diversification to examine, inter alia, this issue. On October 11, 1982, our committee, chaired by Commissioner Stanley York of the Wisconsin Public Service Commission, submitted its report to the full Association, addressing the need for State commissions to monitor utility diversification for the benefit of utility ratepayers.

As one would expect, the focus of the work of our diversification committee was to assess the likely impact of diversification

upon utility ratepayers, and to consider and recommend the development of regulatory policies and procedures to protect such ratepayers. The work of the committee did not focus specifically upon the impact of diversification upon non-ratepayer interests, such as potential competitors of diversified utility businesses. This is hardly surprising, since in every jurisdiction, the primary mission of the State regulatory commission is to foster ratepayer welfare by ensuring that reliable utility service is provided at the lowest possible cost. While the Committee recognized that regulators should expect to hear from firms with which the utility's diversified activities will be in competition, the NARUC has adopted no specific position concerning the issue of the impact of diversification upon the competitors of regulated utilities. Throughout its deliberations, our ad hoc diversification committee focussed on ratepayer impacts, and not the competitive issues to be discussed today.

Utility diversification has indeed become an important and controversial issue in the United States in the 1980's. Utility managers and regulators often have differing perspectives on this issue. Utility managers consider diversification as a potential/partial solution to financial problems, but also must weigh the risks of such ventures to their investors. Regulators seek to effectively monitor utility activities in order to protect the public interest which requires weighing the risks to ratepayers.

The primary goals of a State commission in discharging its primary responsibility to protect the consumers of utility

services with respect to diversified utility activities may be simply stated: 1) to ensure that the ratepayers of monopoly utility services are not called upon to subsidize nonregulated utility businesses, and 2) to ensure that the diversified business activities of a utility do not threaten the financial integrity of the company's utility business. Utility diversification may require a State commission to employ new regulatory tools, but the commission's basic responsibility does not change.

The first goal--the prevention of ratepayer subsidies--is achieved through careful monitoring of a utility's books and records to ensure that a regulatory barrier exists between the utility's regulated and non-regulated businesses. State regulators seek to prevent a utility from supporting its non-regulated businesses with ratepayer funds and to prohibit transactions between regulated and non-regulated sides of the business at non-cost or market-based transfer prices. This regulatory barrier may also be achieved by requiring the utility to structure its operations in a holding company form, or through separate subsidiaries.

State regulators seek to achieve the second goal--preserving the financial integrity of the utility business--by establishing prudent limits to the utility's diversification activities. Clearly, utility diversification into competitive, non-regulated businesses carries the risk of failure, which in turn may threaten the financial health of the entire system, including regulated utility operations. Therefore, State regulators usually prefer

to see utilities diversify in small steps so that losses in competitive areas remain small in relationship to the larger utility business.

As I have noted, the continuing responsibility to protect utility ratepayers may require a State commission to monitor activity in non-regulated businesses in order to ensure that the utility is not using funds collected from ratepayers for utility service to subsidize such non-regulated activities, whether controlled directly or through subsidiaries. In this regard, scrutiny of the utility's books and records and the establishment of standard accounting methodologies have been found to be necessary regulatory tools. .

All of the activities of an investor-owned utility (gas or electric) occur in the private sector, including the regulated provision of utility services. Our diversification committee in its report emphasized the importance of State commission access to the books and records of all utility activities in which ratepayer well-being may be at risk. In the committee's view, effective monitoring of diversified business activities which pose such risks must be reasonably free and timely. That is to say, regulators must be afforded access to all relevant materials at the time when they are needed if continued ratepayer protection is to be afforded.

Another major concern of State regulators is the possibility of cross-subsidization between regulated and non-regulated utility business. Competitors also fear a cross-subsidization with

the utility which could give the diversified operation a decisive cost advantage. Generally, State regulators seek to prevent cross-subsidization by requiring that transactions between regulated and non-regulated utility operations be cost-based or market-based. For example, regulators have required utilities to purchase coal from captive producers (i.e., utility-owned) at the cost of production, or with reference to prices charged by non-affiliated producers.

Cost allocation is generally determined through uniform accounting procedures. The NARUC, for example, publishes uniform system of accounts, which provide guidelines for the assignment of costs into regulated (ratepayer supported) or non-regulated categories. Some common costs, for which precise allocation formulas are difficult to develop, are allocated on the basis of the judgment and expertise of regulators and their staffs.

In addition, many States have so-called "affiliated interests" authority, which enables the respective State commissions to prescribe special accounting and reporting requirements for transactions between utility affiliates. I have attached a breakdown of this authority as an Appendix to my written statement.

Our ad hoc committee designed specific recommendations for our member commissions to consider when adopting a policy as to utility diversification including:

- * placing the burden on the utility to show that diversification is consistent with the public interest and that ratepayers will be protected from unreasonable risk and from involuntarily subsidizing diversified (non-utility) activity;

* reviewing State statutory and administrative powers regarding control of the following aspects of utility diversification: affiliated interest relationships, transactions between the utility and affiliates, accounting procedures, dividend payments, transfer pricing, common cost allocation, holding company formation, and periodic review of the impact of diversification; and

* establishing a policy wherein any utility wishing to diversify is required to prepare a statement of purpose and goals, a description of the corporate organization plan as well as of the proportion of the total business of the holding company that will be represented by the utility, a methodology for allocating common costs, and a plan of review that trigger periodic State commission oversight.

Most State commissions have the legal authority to investigate complaints concerning utility anticompetitive activities to the extent such activities impact upon these commissions' responsibility to protect ratepayers. Therefore, a complainant who alleges and successfully proves detrimental ratepayer impacts of such activities may well obtain relief from a State commission. However, State commissions generally do not have the legal authority to hear and decide pure antitrust disputes containing no clearcut ratepayer impacts, because they have not been provided such authority by their legislatures. In these instances a complainant should look to the State Attorney General to enforce State antitrust laws against anticompetitive utility operations, or consider filing a private antitrust suit under such laws. On the Federal level, such laws as the Sherman and Clayton Acts, the Federal Trade Commission Act, and the Public Utility Holding Company Act (PUHCA) provide the principles to protect against anticompetitive practices. The NARUC has testified before the House and the Senate on the PUHCA, strongly opposing attempts to repeal the Act or to weaken the protection of ratepayer interests which

that Act provides. We are certainly willing to work with our Federal colleagues in dealing with any unfair competition issues. However, we would strongly oppose any efforts to inflict additional Federally imposed restraints upon the ability of the States to protect the interests of utility ratepayers.

This concludes my prepared remarks. Thank you for your time and attention. I would be happy to answer any questions you may have.

APPENDIX

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Table 14 - Special Reporting Requirements

AGENCY	The Agency prescribes special requirements for transactions with affiliates -	
	Accounting	Reporting
FUE and FUEB	Prescribed system of accounts and annual report forms. Requires maintenance and reporting of accounts accounts for investments in advances to, notes receivable from, accounts receivable from, advances from, notes payable to, and accounts payable to affiliates.	Same.
ALABAMA PUC ALABAMA PUC ALABAMA PUC ALABAMA PUC	Yes. Yes. No special requirements established to date. Yes system of accounts and annual reports; also same requirements as FUEB and FUE, where applicable.	Investigation by staff. Yes. No special requirements established to date. Same.
CALIFORNIA PUC CALIFORNIA PUC CONNECTICUT DCR CONNECTICUT DCR	Accounting requirements same as FUEB and FUE. Accounting requirements same as FUEB and FUE. Any special accounting treatment is required.	Same. Same. Service contract changes from affiliates are reported in the utilities' annual reports. Reporting requirements same as FUEB and FUE. The Commission can set those reporting requirements necessary to carry out its statutory responsibilities.
FLORIDA PUC FLORIDA PUC HAWAII PUC HAWAII PUC	Yes. Yes. Notified in rule cases. Approval of all transactions except those specifically excluded by Sec. 8(a) of the Public Utilities Act.	Yes. Yes. Short submit consolidating statements with explanation of transactions and basis of allocation of common expenses. This commission does not have an affiliated interest system. File reports relative to such transactions as the commission may prescribe.
ILLINOIS PUC ILLINOIS PUC ILLINOIS PUC ILLINOIS PUC	Yes. Records of transactions must be preserved in the same manner as for the utility. Summary-differential documentation may be required and pricing is subject to greater scrutiny. Making adjustments for cases of reworking (Statute requires full disclosure).	Yes. Same as FUEB and FUE. Must identify related companies in annual report. File all contracts and keep Commission fully informed of transactions (required by statute).
LOUISIANA PUC LOUISIANA PUC LOUISIANA PUC LOUISIANA PUC	Yes, insofar as certain transactions are concerned. Only as certain require. No special requirements prescribed would follow requirements of the uniform system of accounts and report forms. To the extent that they affect the regulated utility adversely.	Only as commission requires. Requires an abbreviated report from from each affiliate.
MAINE PUC MAINE PUC MAINE PUC MAINE PUC	For system of accounts. For system of accounts. No. Yes. Must be absolutely separate.	Yes, in rate case filing requirements and annual reports. Part of Annual Report. No. Yes. All transactions are kept separately.
MASSACHUSETTS PUC MASSACHUSETTS PUC MASSACHUSETTS PUC MASSACHUSETTS PUC	All transactions deemed necessary by PUC. Depends upon specific transactions. Depends upon specific transactions.	Same. Must submit various contracts which affect the telephone utilities - such as contracts for services rendered and charged to utility. Description required to be given in annual report plus supplemental reports if deemed necessary.
NEW HAMPSHIRE PUC NEW HAMPSHIRE PUC NEW HAMPSHIRE PUC NEW HAMPSHIRE PUC	Transactions must be reasonable and provide for elimination of unprofitable rates. Limited authority under new legislation to investigate certain subsidiary relationships. Companies required to keep accounts so as to be able to accurately and expeditiously produce statements of all transactions with companies.	Commission has authority under its general powers to require any special reports or keep the commission informed.
NEW JERSEY PUC NEW JERSEY PUC NEW JERSEY PUC NEW JERSEY PUC	The type and dollar amount of the goods and services represented by transactions between the regulated company and its affiliates must be identifiable in the books of account of the regulated company. No prescription deemed necessary to date. No special requirements established to date. Commission has authority but no standards have been adopted. See significance in this. As required by uniform system of accounts. No special requirements established to date.	Annually the regulated companies must report the type, dollar amount and the name of the affiliate from which goods and services were received. No prescription. No special requirements established to date. Part of annual report. Commission has authority to require reports. Same.
NEW YORK PUC NEW YORK PUC NEW YORK PUC NEW YORK PUC	Permit detail of costs and so profit between affiliates. Commission has authority to approve acquisition by a public utility of 1 percent or more of the voting capital stock of any corporation. No. Yes. All necessary steps to protect consumers.	File detail of all transactions showing costs and other pertinent items. Require Commission Order within 30 days. No. Yes. Reports and other transactions filed and reviewed by the commission.
NEW YORK PUC NEW YORK PUC NEW YORK PUC NEW YORK PUC	Yes. Yes. Yes. There are no specific provisions in our law on these items but the commission is of the opinion it has adequate authority under the terms of the law relating to accounts and records to prescribe such requirements.	Yes. Yes. Yes. PUC has power to require any special reports to keep it informed. Same.
NEW YORK PUC NEW YORK PUC NEW YORK PUC NEW YORK PUC	Yes. Maintain record of the cost of the services provided by the affiliates and if ascertainable the cost of all items sold to the utility. As required by uniform system of accounts. Highly restrictive. Generally, complete separation of operations with only benefits flowing to utility.	Part of the Annual Report. Yes. All services and things should be provided at cost by the affiliates and annual reports of the cost thereof are filed with the commission. As required by annual reports. Yes. Requirements pertained to basis of each case.

Source: 1982 Annual Report on Utility and Carrier Regulation of the National Association of Regulatory Utility Commissioners, p. 505.

Mr. LUKEN. Would you agree that a small subsidy, such as bill stuffing, could be significant in competition terms?

Mr. GRAY. I think the one thing we need to discuss, or to define, is what a subsidy is. In an economic sense, as long as the utility is paying the marginal costs of that extra piece of paper in the bill, there is no subsidy if that is being charged to nonregulated areas.

Clearly, a small businessman can't compete, since he is not sending bills to every ratepayer in the utility service area as a matter of course. The utility is anyway.

So from a regulatory perspective, there may be no subsidy. It may be perceived clearly by someone trying to compete with that utility as unfair use of the utility's size, of its billing practices, but whether or not that is in fact a subsidy, I think, is open to question.

Mr. LUKEN. Do you work for the association——

Mr. GRAY. Yes, sir, I——

Mr. LUKEN. Or are you a regulator?

Mr. GRAY. No. I work for the association.

Mr. LUKEN. You are a lobbyist; you are a legislative person.

Mr. GRAY. I primarily litigate, but today I'm testifying.

Mr. LUKEN. You are not for the public utilities commission?

In the bill stuffing, I guess we have to assume different factual situations. If there is a separate subsidiary, arm's-length transactions of some kind, in bookkeeping at least, and if the utility did the stuffing and didn't charge the subsidiary for that advertising, or for any of the marginal—we call it—costs, then there would be a relatively small subsidy there.

Mr. GRAY. Yes, sir. Yes, sir, and if that were brought to the attention of a State commission in a rate case, they would say, "No, you are not going to recover those incremental costs through your rates. Those you have to bill to your installation program or your marketing program," or something like that.

Mr. LUKEN. Well, I think I understand what you are saying. It is obviously right, because it agrees with what I thought all along.

Mr. GRAY. I'm glad to hear that.

Mr. LUKEN. Yes, well, a little attempt at facetiousness at this time of the day at least will facilitate the closing of the session.

We thank you very much. I think your statement in the record will be very helpful in showing the attitude of the regulators, and your candid answers to questions have been helpful.

Mr. GRAY. Thank you.

Mr. LUKEN. I want to thank all of those who have come and testified. Mr. Weber and Mr. Gonzalez have both indicated that they are very interested in the subject matter, and I can simply assure you that it is not my intention to drop this where it is, but to study it and to take further action, if possible, in line with the comments that have been made here today.

So this will adjourn the meeting of the subcommittee of the Small Business Committee, and we thank all the witnesses and all those who have attended.

[Whereupon, at 5 p.m., the subcommittee was adjourned, to reconvene subject to the call of the Chair.]

APPENDIX

LETTERS SUBMITTED FOR THE RECORD

**Washington
Natural Gas**
A Washington Energy Company

Donald C. Navarra
Senior Vice President - Marketing

June 4, 1984

Honorable Thomas Luken, Chairman
Sub Committee,
Anti Trust and Restraint of
Trade Activity
Sub Committee - House of Representatives
Small Business Committee
Room 2361 RHOB
Washington, D.C. 20515

Please receive, Honorable Thomas Luken,

my communication for inclusion within the official record to your May 22, 1984 action on Utility Marketing Practices. Several factors that help Small Business people and our customers should be considered. At this point, I am furnishing general information.

1. Small businesses install all merchandise we sell or lease to our utility customers. This has been an effective business relationship.
2. Small businesses that install our merchandise also market their own merchandise which includes appliances, high efficiency furnaces, storm windows, etc. We also have dealer marketing programs. Water heating and conversion burner equipment leased by dealers will be purchased by us for our leasing program.
3. Washington Natural Gas has been a merchandising utility for many, many years. Old photos seemed to be from middle 1800's. Our organization and region has a very competitive opposition. Market sales are necessary to maintain share of market. This share of market for residential is now 31%. To your ears, this may sound low. However, energy market competition here is very tight among electricity, oil, wood and natural gas suppliers. A comprehensive marketing effort in merchandising and leasing by energy suppliers and by dealers is needed.
4. Our corporation was the first utility in the nation to enter the customer conservation market in September of 1973. When we first entered the conservation business, as an example, storm window manufacturers "closed down" in summer time. Due to stimulation of the market, the manufacturers were open year round - the manufacturers and dealers build and install all our window sales. I believe we created a larger market because we sold with competition - and the customer was helped.
5. More efficient gas equipment was also introduced by us to develop the market. As an example, a few years ago, we decided to sell only gas

furnaces with energy efficient electronic pilot systems. The dealers followed suit as market preferences developed. Now - an inefficient furnace would be hard to find and no law for a pilotless furnace was necessary because we saw the future and served the market.

6. Electric competition is favored by new codes and uneconomic purchasing incentives based on "avoided costs". This creates a very difficult competitive environment for heating and water heating. We and our dealers must react or lose business.
7. I noticed a statement about "non utility" activities. A utility can, and sometimes must, market merchandise to provide real markets for small business.

We work with small business people for more business together; together, we have more satisfied customers.

Representative Luken, our marketing concept is to meet customer requirements through the use and support of small business. Their market is stimulated and they service our market as well. Any change would result in less business for the small business people. We would be pleased to provide more information if necessary.

Thank you,



Donald C. Navarre

INDIANA GAS COMPANY, INC.

1630 North Meridian Street • Indianapolis, Indiana 46202-1496 • 317-926-3351

KENNETH L. DEMART
DIRECTOR OF APPLIANCE MARKETING

June 28, 1984

The Honorable Tom Luken, Chairman
Small Business Subcommittee on
Antitrust and Restraint of Trade
U. S. House of Representatives
3239 Rayburn House Office Building
Washington, D.C. 20515

Dear Mr. Luken:

Mr. James A. Johnson, President of Midway Supply Corporation, Seymour, Indiana, made a statement for the American Supply Association before the Subcommittee on Antitrust and Restraint of Trade Committee on Small Business, U. S. House of Representatives on May 22, 1984. Mr. Johnson made reference to policies and programs of Indiana Gas Company that are misleading and in certain cases totally inaccurate.

The following information is being provided for your information in an attempt to clarify and correct certain topics that were covered in Mr. Johnson's presentation.

Indiana Gas Company is an operating public utility in the State of Indiana, is engaged in the business of rendering gas utility service to approximately 314,000 customers in 201 communities, including the community of Seymour, and adjacent rural areas in 46 counties in north central, central and southern portions of Indiana. It is subject to regulations by the Public Service Commission of Indiana (PSCI) in the manner and to the extent provided by the laws of the State of Indiana.

Indiana Gas provides natural gas service to the public by means of gas utility plant, properties, equipment and facilities owned, operated, managed and controlled by the Company which are used and useful for the convenience of the public in the purchase, production, storage, distribution and sale of gas at retail for domestic, commercial and industrial purposes.

In describing Indiana Gas Company's merchandise sales program on page 3 of his testimony, Mr. Johnson states that no credit application or waiting period is involved in buying merchandise from Indiana Gas Company. Indiana Gas Company has a written operating policy which requires a credit check on every applicant before a Merchandise Sales and Security Agreement can be approved.

On page 3, paragraph 4 of Mr. Johnson's testimony he states that the interest rate on merchandise sales is 9.9% for a full year and that the interest rate is below 10% for all three years on not only the unit but the installation cost as well. He showed comparable interest rates on consumer loans in his area for bank consumer loans as being from 16% to 18%. He also states that Indiana Gas Company's interest rates for consumer loans are 20% below the prime rate in his area. These

statements are incorrect. Indiana Gas Company uses a multiplier of 9.9 to determine the interest charge on the amount to be financed per year. If the item is to be financed for two years, the multiplier is 19.8; if for three years, the multiplier is 29.7. These multipliers equate to an annual percentage rate of approximately 17.8% for one year, 17.9% for two years and 17.6% for three years, depending on the amount to be financed and the period of time involved. These annual percentage rates are comparable with rates for bank consumer loans (16-18%) in Seymour, Indiana.

Mr. Johnson's statement on page 3, paragraph 4, fourth line of his testimony reads, "The monthly payment shown at the right Appendix 'I' indicated an interest rate below 10% for all three years, etc." This information is incorrect. The price, monthly payment and correct annual interest percentage rates are as indicated in the following example:

	<u>1 year</u>	<u>2 years</u>	<u>3 years</u>
Installed price of water heater, incl. s/tax	\$257.36	\$257.36	\$257.36
Interest charge one year (9.9 x 257.36)	25.48		
Interest charge for 2 years (19.8 x 257.36)		50.96	
Interest charge for 3 years (29.7 x 257.36)			76.44
Total payments	\$282.84	\$308.32	\$333.80
Monthly payment	\$ 23.57	\$ 12.85	\$ 9.15
Annual percentage rate	17.8%	17.9%	17.6%
Percentage above prime rate (*11%)	61.8%	62.7%	60.0%

*Referenced in Mr. Johnson's statement

Also see attached copy of Merchandise Sales and Security Agreement showing 17.9% APR - Exhibit A.

Indiana Gas Company supports and promotes business for appliance dealers, distributors, contractors and other small businesses in its service area. Merchandise sold by the Company in three of its four divisions is installed and, in some cases, serviced by qualified outside contractors on a bid basis. The merchandise sold by Indiana Gas Company is purchased from distributors and suppliers such as Mr. Johnson's company which contributes to their overall volume of business. Indiana Gas Company also assists dealers and distributors with promotional programs, sales and service training and other assistance programs that are designed to promote and encourage the sale and use of modern energy-efficient gas appliances and equipment.

Indiana Gas Company's merchandise operation is a below-the-line item. All income and expense associated with the operation must be accounted for separately from the gas distribution business. Strict accounting procedures are required by the PSCI to insure that gas rate funds are not used to support the appliance merchandising operation. All utilities in the State of Indiana are subject to control of the PSCI. The PSCI requires that all costs be allocated in accordance with the National Association of Regulatory Utility Commissioners Uniform Systems of Accounts. The PSCI requires annual reports from utilities for their examination to insure compliance with prescribed cost

allocation procedures. Mr. Johnson, on page 5, paragraph 4, stated "there are few written guidelines or policies to govern specifically how costs are to be allocated." Attached as Exhibit B is a sample of how specific the accounting procedures are defined.

Indiana Gas Company operates a below-the-line appliance merchandising operation for the benefit of all of its customers. It serves many small towns and communities and displays and sells energy-efficient gas appliances, or appliances which utilize hot water which hopefully will be heated by gas, in many of these areas. These appliances are promoted and sold in order to retain and improve the Company's base gas load. All customers benefit when base loads are improved. In the absence of high appliance saturations, natural gas prices for space heating and other uses would be higher and would adversely affect all gas users including business and industry. Indiana Gas Company has been selling gas appliances continuously in most of the large communities it serves for many years. However, the Company discontinued appliance merchandising in a few communities, including Seymour, during the gas supply shortages of the 1970s. With a surplus of gas being available in recent years, Indiana Gas has been gradually reinstating appliance sales programs in these communities.

If it were not for Indiana Gas Company's merchandise operation, many consumers in the Company's service area would not have the opportunity to view a full line of modern energy-efficient gas appliances nor would they have a convenient and easy way to buy them. Most appliance dealers do not inventory a full line of gas appliances. One reason is because it is easier and less expensive to install an electric appliance. A plumber is usually not required to install electric appliances which are often sold to the detriment of the consumer because they cost more to operate and are not as energy efficient from a natural energy point of view as gas appliances.

On page 6 Mr. Johnson states, "Utilities can sell appliances at below cost." This is not the case at Indiana Gas Company where gross margins are strictly adhered to and are substantially higher than gross margins for the average member of the National Appliance Retail Dealers Association (NARDA). Actually Indiana Gas Company's higher gross margins benefit local appliance dealers who normally have lower overhead costs, can operate with lower gross margins on a profitable basis and be more price competitive in the marketplace.

On page 7 of Mr. Johnson's testimony he mentions the financing by utilities of weatherization measures at below market interest rates. Indiana Gas Company does have a residential weatherization financing program that is financed at an interest rate that is below normal market rates. The rate is equal to the Company's average cost of capital. The program was included in a PSCI Order and was developed to help low-income and elderly customers to conserve energy and reduce their energy requirements. Energy conserved through the weatherization program will reduce state and federal assistance to low-income families and the elderly with the result that taxpayers as well as gas utility customers could benefit from the program. Indiana Gas Company's weatherization financing program also benefits small businesses and contracting firms as all weatherization materials, supplies and labor are supplied by independent suppliers and contractors. Programs of this type benefit virtually

every gas consumer and taxpayer. The benefits from weatherizing a house will be realized for many years in the future for a small one-time initial investment by the home owner.

On page 9, paragraph 2, Mr. Johnson expresses the benefits of utility cooperative advertising programs, product displays, referrals, etc., to private suppliers and contractors, but suggests that utilities use low-cost financing, rentals, free installations and low-cost maintenance programs to compete with private business. As for Indiana Gas Company, this statement is incorrect. Indiana Gas charges average retail financing rates, passes contractor installation charges on to the consumer and does not have an appliance maintenance contract program. The cost of advertising, including advertising in bill inserts, which promotes specific brand merchandise showing model numbers and prices is charged to the merchandising operation and is not paid for by utility customers.

Mr. Johnson's main concern was the possibility of subsidization of the utility merchandise operation. Apparently he is not familiar with the uniform accounting system that must be followed when allocating below-the-line income and expenses. These allocations are reported to the PSCI each year and are reviewed for compliance. All losses are borne by utility stockholders and cannot be passed on to gas customers.

Indiana Gas Company's merchandise operation is operated for the benefit of the Company and all of its customers. Its programs encourage gas appliance acceptance by consumers. They inform consumers of new gas appliance technology, give them the opportunity to see a complete line of modern gas appliances, are sold at legitimate list prices and creates gas appliance demand which benefits gas appliance distributors and dealers. Gas load from domestic gas appliances forms a utility's base load and improves the efficiency in the use of the Company's assets and benefits all ratepayers. To deny Indiana Gas the ability to improve its operating efficiencies, through improved appliance saturation, and keep its rates as low as possible would not be in the best interest of its customers, suppliers, contractors, appliance dealers or the economy of the State of Indiana.

Very truly yours,

Kenneth L. DeLoach

KLD:sa

Enclosures (2)

to LARRY

cc: Mr. H. C. Spencer
Vice President-Public Relations
Indiana Gas Company, Inc.

EXHIBIT-A

TYPE OF SALE		ADJ.	SALES	NETS	NO.	TAX CODE	TICKET NUMBER	DATE	TIME
CASH ON HAND		0	1	2	3	4	5	6	7
CONTRACT		0	1	2	3	4	5	6	7

SELLER: INDIANA GAS COMPANY, INC.
 BUYER: ANDERSON, LIND
 ADDRESS: 415 JACKSON
 CITY: INDIANAPOLIS
 STATE: IN
 ZIP: 46101

DATE FINANCED: 9/10/1974
 TYPE SALE: 1
 DELIVER: 1
 INSTALL: 1
 MAINT: 1
 COMMISSION: 1
 CREDIT: 1
 NAME: 1
 ADDRESS: 1
 CITY: 1
 STATE: 1
 ZIP: 1

SPECIAL INSTRUCTIONS

SECURITY AGREEMENT

To secure the payment of the indebtedness evidenced herein, Buyer grants to Seller a security interest in the goods being purchased as a part of this transaction, as specifically described as follows:

RP-400 RUUD WATERHEATER
2204 314425
MADISON
2371 W 12th ANDERSON, IND
GREGORY CA-70

which are or may become fixtures on the real estate in MADISON Indiana, hereinafter referred to as REAL ESTATE, and legally described as 2371 W 12th ANDERSON, IND

This security interest shall be governed by the Indiana Uniform Commercial Code. Seller is authorized by Buyer to prepare and file financing statements in and against the real estate described herein, and to execute and file any other documents necessary to perfect its security interest in the real estate described herein.

Buyer hereby agrees to execute and file any documents necessary to perfect its security interest in the real estate described herein, and to execute and file any other documents necessary to perfect its security interest in the real estate described herein.

ITEMIZATION OF AMOUNT FINANCED	
(1) SALES PRICE	2,149.50
(2) DELIVERY AND INSTALLATION CHARGES	274.15
(3) CASH PRICE (SUM OF 1 AND 2)	2,423.65
(4) TRADE IN	
(4A) ALLOWANCE	
(5) AMOUNT SUBJECT TO SALES TAX (3 MINUS 4A)	
(6) SALES TAX	274.15
(7) TRANSFERRED BALANCE FROM PREVIOUS ACCOUNT	137.33
(8) SUB TOTAL (SUM OF 3, 6, AND 7)	2,835.13
(9) CASH DOWN PAYMENT (CASHIER DATE AND INITIAL)	6-4-84 (M)
(10) TOTAL DOWN PAYMENT (SUM OF 4A AND 9)	500.00
(11) UNPAID BALANCE OF CASH PRICE (3 MINUS 10)	2,335.13
(12) AMOUNT FINANCED (SUM OF 8, 7, AND 11)	2,335.13

FEDERAL DISCLOSURES

AMOUNT FINANCED (The amount of credit provided to you or on your behalf)	2,335.13
FINANCE CHARGE (The dollar amount the credit will cost you)	1,147.17
TOTAL OF PAYMENTS (The amount you will have paid after you have made all scheduled payments)	3,482.30
TOTAL SALE PRICE (The total cost of your purchase on credit, including your downpayment of \$ 50.00)	335.48
ANNUAL PERCENTAGE RATE (The cost of your credit as a yearly rate)	17.9 %

REPAYMENT SCHEDULE The "Total of Payments" shown above shall be paid in 124 monthly payments of \$ 1,147.17 beginning on JULY 2 1974, and continuing on the same day of each following month until paid, except the final payment shall be \$ 1,147.17.

CONSEQUENCES: If you pay on time, you may be entitled to a refund of part of the finance charge.

DELINQUENCY: If payment is late, you may be charged:

☐ a delinquency charge.

☐ a delinquency charge not exceeding the lesser of \$11.00 or 5% of the delinquent amount of the installment.

REPOSSESSION: You are giving a security interest in the goods being purchased as part of this transaction. The Seller should refer to the consumer protection laws on the back and reverse of this document for additional information concerning repossession, default, any required prepayment in full before the scheduled date, and liability insurance.

BUYER'S RIGHT TO CANCEL: THE BUYER MAY CANCEL THIS TRANSACTION AT ANY TIME PRIOR TO MIDNIGHT OF THE THIRD BUSINESS DAY AFTER THE DATE OF THIS TRANSACTION. SEE THE ATTACHED NOTICE OF CANCELLATION FOR AN EXPLANATION OF THIS RIGHT. THIS AGREEMENT IS SUBJECT TO ADDITIONAL TERMS AND CONDITIONS CONTAINED ON THE REVERSE OF THIS DOCUMENT. BE CERTAIN THAT YOU HAVE READ THE MATERIAL WHICH APPEARS ON BOTH SIDES BEFORE SIGNING THIS DOCUMENT.

The undersigned understand and agree to all of the terms of this agreement, including those on the reverse of this page, confirm that it was completed, with all blanks filled-in, before signing it and acknowledge receipt of a completed copy of this document. Signed this 1 day of JUNE 1974.

APPROVED: James E. Plan 37-000 353

EXHIBIT B

1976 Revisions Of
Uniform System Of Accounts
For
Class A and B
Gas Utilities
1972



NATIONAL ASSOCIATION
OF
REGULATORY UTILITY
COMMISSIONERS

GENERAL INSTRUCTIONS

1. Classification of Utilities.

A. For the purpose of applying systems of accounts prescribed by the Commission, gas utilities are divided into four classes, as follows:

Class A. Utilities having annual gas operating revenues of \$2,500,000 or more.

Class B. Utilities having annual gas operating revenues of \$1,000,000 or more but less than \$2,500,000.

Class C. Utilities having annual gas operating revenues of \$150,000 or more but less than \$1,000,000.

Class D. Utilities having annual gas operating revenues of \$25,000 or more but less than \$150,000.

B. This system of accounts applies to Class A and Class B utilities. Those applicable to Class C and Class D utilities are issued separately.

C. The class to which any utility belongs shall originally be determined by the average of its annual gas operating revenues for the last three consecutive years. Subsequent changes in classification shall be made when the annual gas operating revenues for each of the three immediately preceding years shall exceed the upper limit, or be less than the lower limit, of the annual gas operating revenues of the classification previously applicable to the utility.

D. Any utility may, at its option, adopt the system of accounts prescribed by the Commission for any larger class of utilities.

2. Records.

A. Each utility shall keep its books of account, and all other books, records, and memoranda which support the entries in such books of account so as to be able to furnish readily full information as to any item included in any account. Each entry shall be supported by such detailed information as will permit ready identification, analysis, and verification of all facts relevant thereto.

B. The books and records referred to herein include not only accounting records in a limited technical sense, but all other records, such as minute books, stock books, reports, correspondence, memoranda, etc. which may be useful in developing the history of or facts regarding any transaction.

C. No utility shall destroy any such books or records unless the destruction thereof is permitted by rules and regulations of the Commission.

D. In addition to prescribed accounts, clearing accounts, temporary or experimental accounts, and subdivisions of any accounts, may be kept, provided the integrity of the prescribed accounts is not impaired.

E. All amounts included in the accounts prescribed herein for utility plant and operating expenses shall be just and reasonable and any payments or accruals by the utility in excess of just and reasonable charges shall be included in account 426, Miscellaneous Income Deductions.

F. The arrangement or sequence of the accounts prescribed herein shall not be controlling as to the arrangement or sequence in report forms which may be prescribed by the Commission.

3. Numbering System.

A. The account numbering plan used herein consists of a system of three-digit whole numbers as follows:

100-199 Assets and Other Debits.

200-299 Liabilities and Other Credits.

300-399 Plant Accounts.

400-434 Income Accounts.

435-439 Retained Earnings.

480-499 Revenue Accounts.

700-899 Production, Transmission and Distribution Expenses.

900-949 Customer Accounts, Customer Service, Sales Promotion, and Administrative and General Expenses.

B. In certain instances, numbers have been skipped in order to allow for possible later expansion or to permit better co-ordination with the numbering system for other utility departments.

C. The numbers prefixed to account titles are solely for convenience of reference and are not part of the titles. Each utility may adopt such plan of account numbers as it deems appropriate; provided, however, that it shall keep readily available a list of the account numbers and subdivisions of accounts which it uses and a reconciliation of such numbers and subdivisions with the account numbers and titles provided herein. Further, the records must be so kept as to permit classification or summarization for each accounting period according to the prescribed accounts.

4. Accounting Period.

Each utility shall keep its books on a monthly basis so that for each month all transactions applicable thereto, as nearly as may be ascertained, shall be entered in the books of the utility. Amounts applicable or assignable to specific utility departments shall be so segregated monthly. Each utility shall close its books at the end of each calendar year unless otherwise authorized by the Commission.

5. Submittal of Questions.

To maintain uniformity of accounting, utilities shall submit questions of doubtful interpretation to the Commission for consideration and decision.

6. Item Lists.

Lists of "items" appearing in the texts of the accounts or elsewhere herein are for the purpose of more clearly indicating the application of the prescribed accounting. The lists are intended to be representative, but not exhaustive. The appearance of an item in a list warrants the inclusion of the item in the account mentioned only when the text of the account also indicates inclusion inasmuch as the same item frequently appears in more than one list. The proper entry in each instance must be determined by the texts of the accounts.

7. Extraordinary Items.

It is the intent that net income shall reflect all items of profit and loss during the period with the sole exception of prior period adjustments as described in General Instruction 8. Those items related to the effects of events and transactions which have occurred during the current period and which are not typical or customary business activities of the company shall be considered extraordinary items. Commission approval must be obtained to treat an item as extraordinary. Such request must be accompanied by complete detailed information. (See accounts 433 and 434.)

8. Prior Period Items

Items relating to transactions which occurred prior to the current calendar year but were not recorded in the books of account shall be included in the same accounts in which they would have been recorded had the item been recorded in the proper period. Such items relate to events or transactions which occurred in a prior period or periods, the accounting effects of which could not be determined with reasonable assurance at the time, usually because of major uncertainty then existing. When the amount of a prior period item is relatively so large its inclusion

for a single month would distort the accounts for that month, the amount may be distributed in equal amounts to the accounts for the current and remaining months of the calendar year. However, if the amount of any prior period item is so large that the company believes its inclusion in the income statement would seriously distort the net income for the year, the company may request Commission approval to record the amount in account 439, Adjustments to Retained Earnings. Such a request must be accompanied by adequate justification.

9. Unaudited Items.

Whenever a financial statement is required by the Commission, if it is known that a transaction has occurred which affects the accounts but the amount involved in the transaction and its effect upon the accounts cannot be determined with absolute accuracy, the amount shall be estimated and such estimated amount included in the proper accounts. The utility is not required to anticipate minor items which would not appreciably affect the accounts.

10. Distribution of Pay and Expenses of Employees.

The charges to utility plant, operating expense and other accounts for services and expenses of employees engaged in activities chargeable to various accounts, such as construction, maintenance, and operations, shall be based upon the actual time engaged in the respective classes of work, or in case that method is impracticable, upon the basis of a study of the time actually engaged during a representative period.

11. Payroll Distribution.

Underlying accounting data shall be maintained so that the distribution of the cost of labor charged direct to the various accounts will be readily available. Such underlying data shall permit a reasonably accurate distribution to be made of the cost of labor charged initially to clearing accounts so that the total labor cost may be classified among construction, cost of removal, utility operating functions, (manufactured gas production, natural gas production and gathering, products extraction, underground storage, transmission, distribution, etc.) and nonutility operations.

12. Operating Reserves.

Accretions to operating reserve accounts made by charges to operating expenses shall not exceed a reasonable provision for the expense. Material balances in such reserve accounts shall not be diverted from the purpose for which provided unless the permission of the Commission is first obtained.

13. Records for Each Plant.

A. Separate records shall be maintained by gas plant accounts of the book cost of each plant owned, including additions by the utility to plant leased from others, and of the cost of operating and maintaining each plant owned or operated. The term "plant," as here used, means each manufactured gas production plant, the wells and gathering lines of each distinct production area, each system of interconnected transmission mains, each system of wells and lines of an underground storage project, each large purification or dehydration plant, each compressor station other than a distribution compressor station, and each products extraction plant.

B. A natural gas company may, with the approval of the Commission, group certain of its systems of gathering lines and wells, small compressor stations, systems of underground storage lines and wells, and systems of interconnected transmission mains for the purpose of complying with the portion of this instruction requiring a segregation of the cost of operating and maintaining each plant.

Note A.—Where manufactured gas is produced by two or more processes at one location, each process shall be accounted for separately.

Note B.—Each natural gas company shall maintain operating or accounting records for each well showing (a) acreage on which drilled, (b) dates of drilling period, (c) cost of drilling, (d) depth of well, (e) particulars and depth of each stratum drilled through, (f) geological formation from which gas is obtained, (g) initial rock pressure and open flow capacity, (h) sizes of casing used and the lengths of each size, (i) total cost of well as recorded in gas plant accounts, (j) date well abandoned, for wells once productive, (k) date transferred to underground storage plant, for wells converted to storage use, and (l) date drilling discontinued, for wells determined to be nonproductive. The foregoing data, as appropriate, shall also be maintained for each subsequent change in the depth of each well.

14. Accounting for Other Departments.

If the utility also operates other utility departments, such as electric, water, etc., it shall keep such accounts for the other departments as may be prescribed by proper authority and in the absence of prescribed accounts, it shall keep such accounts as are proper or necessary to reflect the results of operating each such department.

15. Transactions with Associated Companies.

Each utility shall keep its accounts and records so as to be able to furnish accurately and expeditiously statements of all transactions with associated companies. The statements may be required to show the general nature of the transactions, the amounts involved therein and the amounts included in each account prescribed herein with respect to such transactions. Transactions with associated companies shall be recorded in the appropriate accounts for transactions of the same nature. Nothing herein contained, how-

ever, shall be construed as restraining the utility from subdividing accounts for the purpose of recording separately transactions with associated companies.

16. Contingent Assets and Liabilities.

Contingent assets represent a possible source of value to the utility contingent upon the fulfillment of conditions regarded as uncertain. Contingent liabilities include items which may under certain conditions become obligations of the utility but which are neither direct nor assumed liabilities at the date of the balance sheet. The utility shall be prepared to give a complete statement of significant contingent assets and liabilities (including cumulative dividends on preference stock) in its annual report and at such other times as may be requested by the Commission.

INCOME ACCOUNTS

Note. -Related operating taxes shall be recorded in account 408.1, Taxes Other than Income Taxes, Utility Operating Income, and income taxes shall be recorded in account 409.1, Income Taxes Utility Operating Income, identified separately.

414. Gains (Losses) from Disposition of Utility Property.

A. This account shall include as approved by the Commission, gains and losses from the sale, conveyance, exchange or transfer of utility property to another. (See utility plant instruction 5F, 7E and 10E.) The income tax effect attributable to gains and losses recorded in this account shall be recorded in account 409.1, Income Taxes, Utility Operating Income.

B. This account shall be maintained so that the transactions and details underlying each gain or loss will be readily identifiable.

2. OTHER INCOME AND DEDUCTIONS

A. OTHER INCOME

415. Revenues from Merchandising, Jobbing and Contract Work.

416. Costs and Expenses of Merchandising, Jobbing and Contract Work.

A. These accounts shall include, respectively, all revenues derived from the sale of merchandise and jobbing or contract work, including any profit or commission accruing to the utility on jobbing work performed by it as agent under contracts whereby it does jobbing work for another for a stipulated profit or commission, and all expenses incurred in such activities.

B. Records in support of these accounts shall be so kept as to permit ready summarization of revenues, costs and expenses by such major items as are feasible.

Note - Related operating taxes shall be recorded in account 408.2, Taxes Other than Income Taxes, Other Income and Deductions, and income taxes shall be recorded in account 409.2, Income Taxes, Other Income and Deductions.

ITEMS

Account 415:

1. Revenues from sale of merchandise and from jobbing and contract work.

Revised 1976

INCOME ACCOUNTS

2. Discounts and allowances made in settlement of bills for merchandise and jobbing work.

Account 416:

Labor:

1. Canvassing and demonstrating appliances in homes and other places for the purpose of selling appliances.
2. Demonstrating and selling activities in sales rooms.
3. Installing appliances on customer premises where such work is done only for purchasers of appliances from the utility.
4. Installing piping or other property work, on a jobbing or contract basis.
5. Preparing advertising materials for appliance sales purposes.
6. Receiving and handling customer orders for merchandise or for jobbing services.
7. Cleaning and tidying sales rooms.
8. Maintaining display counters and other equipment used in merchandising.
9. Arranging merchandise in sales rooms and decorating display windows.
10. Reconditioning repossessed appliances.
11. Bookkeeping and other clerical work in connection with merchandise and jobbing activities.
12. Supervising merchandise and jobbing operations.

Materials and Expenses:

13. Advertising in newspapers, periodicals, radio, television, etc.
14. Cost of merchandise sold and of materials used in jobbing work.
15. Stores expenses on merchandise and jobbing stocks.
16. Fees and expenses of advertising and commercial artists' agencies.
17. Printing booklets, dodgers, and other advertising data.
18. Premiums given as inducement to buy appliances.
19. Light, heat, and power.
20. Depreciation on equipment used primarily for merchandise and jobbing operations.
21. Rent of sales rooms or of equipment.
22. Transportation expense in delivery and pick-up of appliances by utility's facilities or by others.
23. Stationery and office supplies and expenses.
24. Losses from uncollectible merchandise and jobbing accounts.

417. Income from Nonutility Operations.

A. This account shall include revenues and expenses applicable to operations which are nonutility in character but nevertheless constitute a distinct operating



National Oil Jobbers Council
1707 H Street, N.W., 11th Floor
Washington, D. C. 20006 202/331-1198

June 22, 1984

The Honorable Thomas A. Luken
Chairman
House Small Business Antitrust Subcommittee
B 363 Rayburn House Office Building
Washington, D. C. 20515

Re: NOJC Comments on "Utility
Competition with Small Business
Owners" Hearings Held May 22,
1984.

Dear Mr. Chairman:

The National Oil Jobbers Council commends you and your Committee for addressing the competitive implications of utility activities on the small business sector. Clearly, small business fuel oil marketers are being adversely affected by certain gas and electric utility practices.

The National Oil Jobbers Council is a federation of 42 state and regional trade associations representing thousands of independent small business petroleum marketers. Collectively, our members market approximately 5% percent of the motor fuel and 85 percent of the home heating oils sold in the United States. Though we market large volumes of petroleum products, we are, nonetheless, individually small within the industry.

Independent distributors of petroleum products, specifically retail home heating oil marketers, are finding their small businesses disrupted by the entry of publicly regulated utilities into the private sector. This "venturing" of utilities into a competitive marketplace, where in most instances the utility is protected from competitive market forces because of its monopoly status, has forced some fuel oil dealers out of the marketplace and placed many more at a tremendous competitive disadvantage. This has generated significant activity and concern among fuel oil marketers. The NOJC appreciates the opportunity, through these comments, to express those concerns.

Marketer Concerns About Fuel Switching

One of the major concerns of fuel oil marketers is the problem of utilities promoting fuel switching by utilizing a federal program to promote the conversion of oil heated homes to whatever fuel the utility markets. The National Energy Conservation Policy Act (NECPA), as amended by the Energy Security Act, prescribes programs - the Residential Conservation Service (RCS) program and the Commercial and Apartment Service (CACS) program - which require natural gas and electric utilities to offer low cost energy audits to residential, commercial and apartment dwellings. Utilities can use the federal RCS and CACS mandate to promote fuel switching.

There is simply not adequate protection built into the RCS or CACS programs to guard against a utility taking unfair advantage of a fuel oil consumer or building owner enticing him/her to switch to the utility's energy source. This is particularly ironic given that the objective of these programs is to promote conservation and the most efficient utilization of all fossil fuels, not increased consumption of one fossil fuel over another. A utility operating under either of these programs has a strong incentive to encourage fuel oil apartments and commercial buildings to convert to natural gas or electricity, and thereby expand its customer and resource base.

The RCS and CACS programs should be limited to the utility's existing customer base. At the very least, if a utility is required to offer an auditor to all oil heated homes, apartments and commercial buildings, they should be required to notify the home heating oil marketer serving that customer that the utility auditor has inspected the current oil system.

Diversification

Within the past several years, natural gas and electric utilities have increasingly taken advantage of their monopoly position in the marketplace to expand this resource base. The utilities, in an attempt to generate more revenue and increase their customer base, have extended their interests to include not only the production and distribution of energy but also the sale, installation, and service of gas and electric appliances, products, and systems. The monopolization of the energy market threatens the very existence of small business fuel oil marketers, many of whom provide such services.

As a regulated entity, the utility enjoys numerous advantages over the small businessman. Utility companies under the auspices of a regulated monopoly status are protected from the usual risks of doing business in a competitive marketplace—risks that must be faced by competing businesses. Utilities, in addition, have various financial resources on which to rely and may use profits that have been generated from their regulated, monopolistic status unfairly. These and other advantages allow utilities to sell commodities at below competitive prices of their competitors.

Predatory Pricing

While gas and electric utilities in most instances face little direct competition from other utilities, they do face competition from alternative fuels. Currently, natural gas utilities are concentrating on the "dual fuel" market which they fear will be lost due to competition from other fuels, particularly fuel oil and coal.

In recent months, natural gas utilities throughout the country have been seeking authority from state public utility commissions to offer special discount rates for "dual fuel" customers. These are customers who are capable of switching from gas to oil or coal depending upon the economics of the relative fuel costs. The applications request either a flexible rate to be

established by the utility on a month-to-month basis to undercut the competitive price of fuel oil, or a discount from the existing interruptible rate sufficient to reduce the interruptible gas rate below the competitive fuel price.

This type of predatory pricing is pushing fuel oil out of existing markets and is preventing fuel oil from entering potential markets. These pricing policies, while used today predominantly in the industrial or commercial dual-fuel market, could very easily be adopted to residential markets.

Promotional Activities of Gas and Electric Utilities

Although the regulated natural gas price advantage over deregulated fuel oil has been reduced in many markets, utilities are looking at increased promotional activity geared toward making the natural gas industry more attractive to the consumer. Gas utilities want to be able to offer to their customers "one stop shopping" and change their image.

Promotional programs employed by utilities include special rebates and inducements to customers to encourage their conversion from oil. In one recent case, the utility offered low-cost financing, a free three year service policy, and \$200 rebate per customer for equipment replacement, and other incentives totalling hundreds of dollars if a consumer not currently served by that utility would replace his or her oil system with natural gas. Cumulatively, these special payments amount to millions of dollars in below-cost service, financing, and deals offered to builders and developers in the new home market. These costs may generally be absorbed by the consumer.

The utility industry also implements advertising strategies that many times incorporate false and misleading information in an effort to attract oil customers to natural gas. Ads which state that "gas is the most economical heating source" or, "gas is the most efficient" are common examples. These ads overstate the true costs and understate the efficiency of fuel oil. Department of Energy studies consistently show that fuel oil systems are more efficient than gas systems.

Utility Stockholders Should Bear Risks

Where a utility subsidizes its prices to one class of user (such as interruptible) by charging additional rates to other classes of users (firm customers), the firm customer often bears the risk associated with the rate design. The utility often just shifts the risk in order to hold prices to one class of customers at artificially low levels. If a state regulatory commission is going to permit a utility to cut its rates to interruptible customers, the risk of recouping these potential lost revenues caused by reduced rates should be shifted to the utility stockholders, not the firm customer base as is currently the case.

Conclusion

The home heating oil market is extremely competitive. In that market, consumers have the choice of purchasing product from a dealer who also offers regularly scheduled furnace repair and maintenance or the consumer can shop around and purchase product from other fuel oil companies. Home heating oil marketers compete not only among themselves, but also with fuels such as natural gas and electricity provided by utilities which receive a fixed rate of return on their investments.

NOJC believes that the consumer should be a primary concern of the regulators and that the small business person's competitive interests should be taken into consideration as well. There must be additional accountability and simplification of the utility regulatory process so that small business interests can be adequately represented in state proceedings. Inadequate notice by utilities, the expense of participating in the regulatory process, lack of a definitive answer once a participant, the ability of the utility to subsidize one part of its business with resources from another, government programs like CACS which although well intended, jeopardize small business interests, are all elements that lead to potentially anti-competitive utility practices.

We urge the Subcommittee to continue to vigorously explore these practices and to continue to carefully analyze their impacts on small business interests.

Sincerely,



Mark O. Decker
Vice President - Policy

MOD/tdm



MANUFACTURING CO.
102 S. 26TH ST. / TACOMA, WA 98402
(206) 272-2900

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LARRY

June 6, 1984

Honorable Thomas Luken
Chairman-Sub Committee
Anti-Trust and Restraint
of Trade Activity
Sub-Committee-House
Small Business Committee
Room 2361 RHOB
Washington D.C. 20515

Dear Sir:

Solar Manufacturing Company has been providing a full-service program to Washington Natural Gas Company of Seattle, Washington, for eight years. During that time, sales and other stimulus provided by Washington Natural Gas have assisted Solar Manufacturing in achieving success as a manufacturer and state-of-the-art window products. Washington Natural Gas' strict marketing policies have assured their customers lasting service: Solar Manufacturing provides warranty services going back to day one. Washington Natural Gas' success is Solar Manufacturing's success.

During the past eight years, we have found Washington Natural Gas customers to be pleased with the care and consideration bestowed upon them by Washington Natural Gas' sales representatives and marketing staff, as well as the product and service guaranteed by Washington Natural Gas' participating contractors.

Solar Manufacturing participates on ten utility conservation programs. The nine electric utility programs suffer continuously from poor products and installations and contractor misrepresentation, due to their own lack of knowledge and skilled management. Contractors are typically paid for their services after 60 to 180 days. Washington Natural Gas pays their participating contractors weekly, allowing for superior service and quality.

As a long-standing, successful business, Solar Manufacturing would like to see more private utility marketing and less public utility give away programs. There is no incentive to a contractor or manufacturer to perform services for a program knowing it will not receive payment within thirty days. There is no incentive for a consumer to participate on a program providing inferior products and service.

Washington Natural Gas customers are assured quality products with long service life. As a consumer, I can think of no better offering on the marketplace. As a manufacturer, I can think of no superior way of providing product and service to the consumer.

Sincerely,

William M. Whelan

William M. Whelan
General Manager

CALL TOLL FREE: 1-800-426-7948 WA. WATS: 1-800-562-6045



Blue Flame Service

PHONE 632-7600

"MATCHLESS" GAS INSTALLATIONS AND SERVICE

611 NORTH 35TH STREET
SEATTLE, WASH. 98103

June 6, 1984

Honorable Thomas Luken
Chairman-Sub Committee
Anti Trust and Restraint
Trade Activity
Sub Committee-House
Small Business Committee
Room 2361 RHOB
Washington, D. C., 20515

Dear Chairman:

We wish to enter into the Official Record our feelings about the May 22nd meeting concerning "Utility Marketing Practices."

As a Dealer and Installer of Gas Equipment we and the Public are best served with the Utility being active in Marketing equipment. They provide the Dealer with the expertise to market new equipment and the Public with Lease and financing programs that small business could not provide. Their advertising campaigns cause healthy competition and accelerates our sales.

I urge you to vote in the Utilities favor.

Sincerely,

James Marsac

JM:pm

c.c. -
Don Navarre
Chuck Harper.



CHARLES CENTER • P. O. BOX 1475 • BALTIMORE, MARYLAND 21203

SIDNEY C. MILLER, JR.
ATTORNEY

June 12, 1984

Honorable Tom Luken
Chairman: Small Business Subcommittee On
Antitrust and Restraint of Trade
Room 3235 RHOB
U. S. House of Representatives
Washington, D. C. 20515

Dear Congressman Luken:

Although we were not present at the May 22 hearing at which evidence was given with respect to the competition between small businesses and the utility industry - we understand that one of the witnesses had occasion to mention Baltimore Gas and Electric Company during the course of his testimony on cross-examination.

If our information is correct, the witness objected to the fact that our Company sells water heaters directly to its customers thereby allegedly placing us in competition with the efforts of a local home improvement company located in the area between Washington and Baltimore.

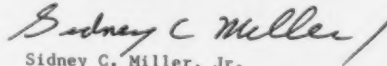
Our Company has been selling gas and electrical appliances to the public since shortly after the turn of the century. This activity was undertaken at that time for a variety of reasons. As you might imagine, one of our primary motivations was to encourage greater utilization of our prime commodities, gas and electricity. Equally important was the desire to provide our utility customers with a knowledgeable and technically competent distributor of all types of household appliances and equipment who would be in a position to provide consistently reliable service for the merchandise which was sold.

Baltimore Gas and Electric Company is fully conscious of the potential advantage which its greater size and resources could give it over smaller merchants. For that reason, to ensure that no unfair competitive advantage is taken, the Company has consistently and deliberately priced its appliances and household equipment at slightly more than the going market rate. Baltimore Gas and Electric Company does not engage in discount merchandising - and has no intention of competing in terms of price with any other retailer, large or small.

As an inducement to the public, the Company offers only good merchandise backed by fully qualified sales and maintenance personnel. Those who elect to buy from Baltimore Gas and Electric Company do so only because of its reputation for good service, reliability and fair dealing. We do not believe that such a reputation should give grounds for complaint to any other competitor.

Thank you for this opportunity to make our views known to your Committee.

Yours very truly,



Sidney C. Miller, Jr.
Attorney for
Baltimore Gas and Electric Company

SCM:prg



June 5, 1984

RICHARD C. VIERBUCHEN
EXECUTIVE VICE PRESIDENT

The Honorable Thomas A. Luken
Chairman
Subcommittee on Antitrust and Restraint
of Trade Affecting Small Business
B-363 Rayburn House Office Building
Washington, D.C. 20515

Dear Chairman Luken:

On Tuesday, May 22, 1984, the Subcommittee on Antitrust and Restraint of Trade held hearings on regulated monopolies' competition with small businesses. During those hearings, one of the witnesses, Mr. Bill Greene of the National Association of the Remodeling Industry (NARI), made inaccurate comments regarding activities of the Washington Gas Light Company and its subsidiaries and divisions in unregulated businesses.

We feel it is imperative that we respond to those comments made in Mr. Greene's testimony. It is respectfully requested that our enclosed statement be included as part of the record so that any action your committee deems appropriate may be properly based on a full representation of the facts.

If we can provide your subcommittee with any additional information, please contact me. You may depend on our utmost cooperation.

Cordially,

R. C. Vierbuchen

Enclosure

Statement for the Record of
Washington Gas Light Company
Submitted to
Subcommittee on Antitrust and Restraint of Trade
of the
Committee on Small Business
U. S. House of Representatives
on
Regulated Monopolies Competition with Small Business
May 22, 1984

Description of Washington Gas Light Company's (WGL) Corporate Structure

WGL is a gas distribution utility serving the metropolitan area of Washington, D.C. Its gas distribution operations are regulated by the Public Service Commissions of the District of Columbia and Maryland and the State Corporation Commission of Virginia. These commissions as well as the Federal Energy Regulatory Commission prescribe the accounting practices that WGL must follow. As a public corporation WGL must keep accounting records which comply with generally accepted accounting principles as certified by independent auditors, and is subject to the regulations of the Securities and Exchange Commission and the New York Stock Exchange.

The retail rates charged for gas utility service are approved after hearings by the above-named public service commissions. Such rates reflect: (a) the allowed return determined by a percentage rate of return applied to the rate base (plant, equipment and working capital) found by the respective agencies as used to serve gas customers; (b) operating and maintenance expenses to provide gas service, including gas purchase costs; (c) depreciation on the plant and equipment; and (d) local, state and federal taxes, including income taxes on the allowed return. This ratemaking procedure precludes ratepayers from being charged for expenses not incurred in providing gas service.

WGL has several wholly owned subsidiaries engaged in energy-related activities. Frederick Gas Company and Shenandoah Gas Company are gas distribution utilities whose accounting practices and retail rates are regulated by three state commissions. Hampshire Gas Company primarily operates a gas storage facility in West Virginia regulated by the Federal Energy Regulatory Commission and engages in limited exploration and production activities in the Appalachian area. Crab Run Gas Company is engaged in gas exploration and production in parts of Oklahoma, Louisiana and West Virginia. The accounting records of these subsidiaries are kept separately from the records of WGL.

As discussed more fully below, Davenport Insulation Company, Inc. is a WGL subsidiary in the insulation business. WGL also has three divisions: Energy Conservation Systems, Commercial Energy Systems, and Air-Conditioning Systems. The activities of these divisions are described in detail below. They are not supported by WGL's utility operations or utility ratepayers.

Davenport Insulation

Davenport Insulation was acquired by Washington Gas in 1977 and represents an investment by WGL shareholders. The books and records of Davenport are kept separate from those of WGL. Its acquisition was not financed by WGL ratepayers. No property of Davenport is included in the rate base of WGL and none of its operating and maintenance costs are included in the regulated cost of service of WGL.

At the time of acquisition, Davenport was primarily involved in insulation supply and installation and has since expanded into storm windows. Its principal market is residential and small- to medium-sized commercial new construction.

While this subsidiary incurred losses during 1978-81, it must be emphasized that those losses were borne solely by WGL shareholders. And, at no time has any risk of this investment been shared by WGL ratepayers. Accordingly, the profits realized by Davenport in 1982-83 were allocated to the WGL shareholders. Strict accounting procedures required by the three public service commissions regulating WGL insure that the costs of Davenport's operations are separately maintained so as to preclude cross-subsidization.

Moreover, advertisements of Davenport Insulation do not state, directly or implicitly, that it is affiliated with WGL. In addition, WGL has not engaged in the promotion of this subsidiary and has not used nor intends to use inserts in monthly gas bills to announce or promote such affiliation or services. In sum, all advertising and promotion activities are initiated, developed and paid for by Davenport.

Energy Conservation Systems

Energy Conservation Systems (ECS) is a separate division of WGL, erroneously cited in Mr. Greene's testimony as a subsidiary. This division was formed in response to the serious interstate gas supply shortage in the 70's, at which time WGL's pipeline suppliers curtailed all of its customers, including WGL. As a consequence, the state commissions which regulate WGL ordered a moratorium on gas hook-ups. Many gas customers, including schools and hospitals were curtailed. New pipeline gas supplies were simply unavailable. WGL, therefore, turned to the promotion of conservation techniques in an effort to alleviate the supply shortage. In that sense, conservation represented an alternative source of supply. ECS was formed in 1975 as a separate division to implement the company's conservation efforts. Its operating and capital costs are kept separate from WGL's utility services; the state commissions accounting regulations insure this separation.

ECS is engaged in the promotion, sale and installation of insulation, storm windows and doors, thermal walls and roofing, ventilation systems and kitchen remodeling products. Its main market has been and continues to be existing residential structures with emphasis on improving energy conservation in the home through the use of superior quality materials.

It is important to note that small area contractors are used exclusively by ECS for its installation activities. In the case of insulation, ECS subcontracts with small businesses to supply both the materials and the labor. To ensure the use of high quality materials, storm windows and doors and thermal siding are purchased directly from the manufacturers but local small contractors are used to install these products. Roofing materials and ventilation systems are purchased from local distributors but, again, local small contractors do all of the installation.

ECS' involvement in kitchen remodeling was limited to cooperation with local appliance dealers to promote the use of high efficiency gas appliances as part of a total remodeling package. This program is being discontinued effective June 1984 because it did not achieve expected profit levels.

Since its inception, ECS activities have actually expanded the size and volume of the conservation supply and installation market. Rather than limiting competition, the ECS division has generated additional business opportunities for many small businesses through the promotion of conservation techniques and through its subcontracting policies. In short, ECS performs a marketing function for its subcontractors.

Advertising for ECS is initiated, developed and paid for by ECS, including newspaper, radio, direct mail, the yellow pages and bill inserts. In the case of the latter, any costs associated with the mailing and insertion of ECS materials are also charged directly to ECS and are not borne by the ratepayers.

ECS does offer financing arrangements for customers that purchase its products. Again, associated credit, accounting and administrative costs are charged directly to the ECS division accounts. The annual percentage rates are competitive with those available on the open market, presently ranging from 13.55 to 15.99%. It is significant to note that, unlike local contractors, the risk of non-payment is borne strictly by ECS. Competing contractors do not bear such a risk since they are paid in full upon contract completion by the customer or the customer's bank which has financed the conservation improvements.

While the customer may utilize his or her gas bill as a convenient means to pay a monthly installment, such payment is first credited to gas service before the balance is applied to the conservation products or services purchased. Moreover, a percentage of the revenues of each ECS contract is used to reimburse WGL for all credit and accounting services that ECS uses in this manner. This reimbursement actually benefits WGL ratepayers because it reduces personnel costs which otherwise would have been paid through utility rates.

Commercial Energy Systems

As in the case of ECS, Commercial Energy Systems (CES) is a separate division of WGL. Administrative and operating costs are charged to CES accounts directly and are not borne by WGL ratepayers. Formed in April 1983 to service the needs of the medium to large commercial, industrial and institutional communities, CES designs and sells total energy management systems. The purpose of CES is to design the most efficient energy system at the lowest cost and best

economics for a particular user. Given this purpose, the emphasis is not necessarily on gas equipment. Rather, the emphasis is on component replacement, waste heat recovery, physical plant lay-out, lighting and computerized energy usage controls which are all components of such a system design.

When CES submits a bid for the installation of an energy management system, a thorough engineering review and evaluation is performed of the existing facilities. CES personnel perform these services with the aid of outside consulting engineers when necessary.

Once a bid has been accepted, CES subcontracts all of the installation work. Materials are typically supplied by local subcontractors and suppliers with the exception of Andover Controls® and Conservalite® equipment, for which CES is the local representative. CES also provides a five-year warranty of the system and subcontracts with local small businesses for any service required under these warranties.

It should be emphasized that the total energy management system concept is a relatively new one and is a rapidly growing business. Competitors in this innovative field include A.T.&T., Honeywell and Johnson Controls as well as numerous local contractors. As with ECS, the activities of CES serve to increase the awareness and acceptance of this new approach to energy conservation. Thus, its activities enhance competition in the energy conservation system market and generate additional business for the many local contractors employed in the installation and servicing of these systems.

A total energy management package may be financed through a straight purchase contract, installments or a service contract. CES offers financing arrangements for purchasers at finance rates that are competitive with open market rates. In the case of a service contract, CES installs and retains title to the equipment for a fixed term and insures operating savings to the customer. All administrative expenses associated with financing are charged to CES and are not borne by the ratepayers.

Air-Conditioning Systems

Air Conditioning Systems (ACS) is also a separate division of WGL funded by shareholder funds. Its main purpose is to promote, distribute and sell state of the art gas heating and air conditioning systems for the commercial community, with major emphasis on Yazaki® double-effect absorption refrigeration systems.

Such commercial air conditioning equipment has historically been provided by Arkla. Since Arkla is no longer manufacturing and supplying this equipment, ACS was formed in June 1983 to meet the supply need thus created so as to replace obsolete or outworn commercial size gas heating and air conditioning systems.

The administrative, operating or promotional expenses of ACS are not borne by the WGL ratepayers. Nevertheless, the development of off-peak,

air conditioning load will actually benefit ratepayers since some of WGL's fixed costs that are presently borne by existing residential and commercial customers will be spread over a larger revenue sales base.

ACS works with local small contractors and dealers to distribute and install this highly efficient equipment. All sales made by ACS are installed by small business contractors in the area. Moreover, ACS provides training to interested contractors wishing to become dealers of these products.

As with ECS and CES, financing is available through ACS. But again, the rates are comparable to those commercially available. Associated administrative expenses are strictly borne by ACS. The risk of non-payment is also the responsibility of ACS and not charged to WGL ratepayers. If a customer chooses to use the monthly gas bill to pay the installments due, mailing, accounting and credit services are also charged to the ACS account.

RCS/CACS Programs

The Residential Conservation Service (RCS) and Commercial and Apartment Conservation Service (CACS) Programs were repeatedly cited during the hearing as prime examples of unfair utility competition. We wish to repeat our long-standing position in support of repeal of both these federally-mandated programs.

WGL's experience with the RCS audit program in Maryland has been dismal, having a cumulative response rate of 2.8% over the past three years. During this period, conservation rates in Virginia parallel those in Maryland— 15 1/2 to 16%—even though no RCS audit program is yet available in Virginia. The federally imposed maximum charge of \$15 per audit is substantially below the \$130 actual cost of performing an RCS audit cost. The differential is paid by all WGL Maryland ratepayers through their rates, even though the vast majority of them have not utilized this service.

It is for these reasons that we do not consider the RCS program cost-effective and believe it should be discontinued before a similar service must be offered in Virginia under federal-standby authority. Moreover, this audit service is available through many small businesses but who are precluded from doing so because they cannot compete with the \$15 federally-mandated maximum charge.

It should be emphasized that there is no interface between the RCS operations and WGL non-utility divisions or Davenport. The list of contractors available to install RCS conservation recommendations is compiled by the state agency and must be distributed to all those customers who have an audit performed. Under the Maryland RCS plan, Section 307(e)(4), WGL is also required to disclose to the customer its association with Davenport and ECS on a separate statement of interest sheet. All audit results and customer contacts are treated as proprietary information of WGL and, therefore are not used to identify potential customers for Davenport or ECS. In short, all RCS activities are conducted in strict compliance with the federal law and the Maryland RCS plan and are subject to the scrutiny of the Maryland Public Service Commission.

Conclusion

All three divisions, ECS, CES and ACS, operate out of a building that is entirely separate and apart from buildings that house WGL's gas utility operations. The leasing costs as well as all telephone service is charged directly to ECS, CES and ACS operating expenses. In short, these divisional operations are separated, both physically and financially, from the gas distribution utility operations of WGL. Advertising, mailings or promotion costs of these divisional operations are directly charged or allocated to the respective division. None of the capital investment (plant or equipment) or operating costs are included in WGL's rate base or in its rates. Thus the ratepayers of WGL, including those in Maryland, bear none of these costs. Moreover, it is apparent that WGL's entry in this functionally related, conservation market has served to enhance competition, not restrict it, and to expand, not limit, business opportunities for small businesses.



american
consulting engineers
council



UNITED STATES MEMBER

File 775.08

1015 FIFTEENTH STREET, N.W., WASHINGTON, D.C. 20005-2670 ☐ (202) 347-7474
Telex: 897445 AMCONENGRC WSH

May 22, 1984

The Honorable Thomas Luken
Chairman
Subcommittee on Antitrust and Restraint of Trade
U. S. House of Representatives
Washington, DC 20515

Dear Mr. Chairman:

We request that this letter concerning utility competition with consulting engineers be included as part of the hearing record of May 22.

The American Consulting Engineers Council (ACEC) is a federation of 51 state and regional Member Organizations that represents over 4000 consulting engineering firms nationwide. ACEC members, in order to assure total objectivity of design to their clients may not have a financial interest in any product included in their specifications.

A significant portion of utility competition to consulting engineering firms is caused by the Federal government. The Residential Conservation Service (RCS) and Commercial and Apartment Conservation Service (CACS) programs require the utilities to offer energy audits to residences, apartment and commercial buildings. That is the business of consulting engineers, except that we have no Federal mandate. We must convince owners to have their buildings audited by consulting engineers instead of utilities---a difficult task made more difficult by the presence of Federal programs. And it is not only consulting engineers who are suffering from this statutorily required competition. Mechanical and electrical contractors, air-conditioning, plumbing, heating and cooling contractors, and more, are all adversely affected by this situation. These professions are almost exclusively small businesses, which makes the problem relevant to this Subcommittee. Enclosed is a fact sheet on why these programs should be repealed.

Competition from utilities also extends into other areas that affect consulting engineers. We believe that with the overall slowdown in the construction of new power facilities, utilities are left with a surplus of unused engineering talent. Some are trying to utilize that talent by doing engineering consulting work for other utilities and anyone else who might have occasion to use them. Enclosed are examples taken from various publications.

President SHELBY K. WILLIS Salina, Kansas • Senior Vice President VERNON B. SPALDING, Madison Heights, Michigan
Vice Presidents PAUL C. BUCKNAM, JR. Wellesley, Massachusetts • L. LEROY CRANDALL Los Angeles, California
CHRISTOPHER MARK New Haven, Connecticut • LESTER H. POGGEMEYER Bowling Green, Ohio • RICHARD L. WILLIAMS Roanoke, Virginia
Treasurer ARNOLD L. WINDMAN New York, New York • President-Elect CLIFFORD E. EVANSON Glenview, Illinois
Executive Vice President LARRY N. SPILLER • Managing Director BRUCE E. VOGELSINGER

While we do not and cannot object to fair competition from whatever source, we are, however, concerned about engineering services offered by utilities and subsidized by the consumers. The Government has granted utilities certain antitrust privileges. We do not believe the utilities should take advantage of these privileges by undertaking new business enterprises and competing with firms who do not enjoy similar privileges. Moreover, the elimination of some of these efforts to compete with other business and concentration on providing the service to the community which was originally required of them, would be in the best interests of all parties involved.

Yours very truly,

Edward R. Bajer

Edward R. Bajer
Director
Energy Division

erb/ssc
enclosures

FEDERAL ENERGY CONSERVATION PROGRAMS HURT SMALL BUSINESS

The Alliance for Fair Competition is a coalition of sixteen national associations representing over one hundred thousand small businesses. Its main purpose is to combat unfair competition from utilities.

The AFC supports repeal of the Residential Conservation Service (RCS) and the Commercial and Apartment Conservation Service (CACS) because they are federal programs that give utilities an unfair competitive advantage in the energy conservation business. Both require gas and electric utilities to give below-cost energy audits to residences, small commercial and apartment buildings.

The AFC support of repeal of these mandatory federal programs should in no way be construed as anti-conservation. On the contrary, member firms are so heavily involved in this industry that it is unnecessary for the government to enact regulatory programs. Competition is fierce. U.S. Government stamp of approval of utility energy conservation programs serves only to give them an unfair competitive advantage.

In addition:

A. By law, a utility can only charge \$15 for an RCS audit. The median cost per audit on a national level is \$134. The difference must be shouldered by the ratepayers.

B. All ratepayers, including low income, pay for RCS through the rate base. However, most participants are middle and upper income, which results in an unfair burden on low-income ratepayers.

C. The RCS, and subsequently the CACS, will require a bureaucracy at the federal level, the state level, and in the utility, to run them. Federally backed utility programs also have a chilling effect on new small businesses entering this market.

D. Other energy conservation programs, like Weatherization and Low Income Energy Assistance, have a much better record of energy savings and are targeted at those who need the help most.

Detroit Edison subsidiary specializes in consulting

Detroit — Detroit Edison will soon be offering engineering, design and related consulting services to electric utilities and other businesses.

To market these services nationally, Detroit Edison has formed a new subsidiary — Utility Technical Services Inc. Walter J. McCarthy Jr., chairman and chief executive officer of Detroit Edison, will serve as the subsidiary's chairman.

— UTS will sell consulting services using Detroit Edison experts — temporarily working for the subsidiary — and will market the use of developed programs, systems and equipment. Engineering consulting services will be provided initially to small and medium-sized electric utilities in the continental United States, but will not be limited to that market.

Services will include power plant design assistance, boiler computer modeling, plant operation problem-solving, related engineering laboratory testing and technical training.

UTS will advise in automated mapping to units of government, energy companies and communications companies nationwide. It will design complete automated mapping systems and computerize clients' existing maps and related records.

George O. Murray and Chester J. Bolling have been named UTS managers. Murray will be responsible for engineering consulting activities, and Bolling will be responsible for computer graphics activities.

Murray most recently headed Detroit Edison's New Technology Marketing unit. Bolling headed a Detroit Edison Project Development unit.

The board of directors of the new subsidiary, in addition to McCarthy, include: Charles M. Heidel, president and chief operating officer; Harry Tauber and Burkhard H. Schneider, group vice presidents; and Whiddon and Willard R. Holland, vice presidents. UTS officers are Whiddon as president, James J. Gesaner and Ronald L. McIntyre, vice presidents, and Frank D. Stellingwerf, secretary-treasurer.

TVA Plans \$100,000 Job Boost Program

The Tennessee Valley Authority plans to pay a total of \$100,000 to local companies to hire and train the unemployed as part of a continuing effort of the federal agency to help combat the unemployment problem in this area.

Participating firms will receive \$450 for every worker taken off the unemployment rolls and put into the workforce.

During the past year TVA spent \$100,000 to create 1,300 jobs through a similar effort in North Georgia, making such an impact that the state set aside federal Appalachian Regional Commission funds to continue the program.

"We took people off the unemployment rolls and put them into productive work," said TVA program manager Tom Rogers.

"When you add up all the contribu-

tions they make and subtract all the money saved the federal government, the benefit-cost ratio is about 39-1."

Estimated economic benefits totaled \$1 million as a result of that effort, according to TVA statistics.

Seven cities will be included in this job program effort, which will be administered through local power authorities.

Free civil engineering and architectural work will also be available for firms planning to expand their physical plants.

Distributors involved in the program include the Electric Power Board of Chattanooga, Morristown Power System, East Mountain Electric Cooperative, Cumberland Electric Membership Cooperative, Warren Rural Electric Co., Alcorn County Electric Power Association and Jackson Electric Utility.



623-1060, Ext. 2231

THE
ILLUMINATING
COMPANYPUBLIC RELATIONS
PO BOX 2230
CLEVELAND, OHIO 44101

L-62

November 9, 1983

FOR LICENSEE REEL-SI

NEW COMPANY FORMED TO MEET
ELECTRIC ENERGY NEEDS

Dynamic Energy Ventures, Inc. is one of Cleveland's newest companies, but it's an outgrowth of one of the oldest firms in all of Cleveland-Northeast Ohio.

The new company is a subsidiary of the Cleveland Electric Illuminating Company, which has been providing electricity for over 100 years. The new firm, created by the CEI Board of Directors in September, will provide expanded services to CEI's customers.

Robert M. Ginn, Illuminating Company chairman, said Dynamic Energy Ventures was formed in recognition that many customers have new and changing energy needs.

"The new business will furnish those customers with energy-related options beyond those normally offered by an electric utility company," he said.

Gary Greben, president of the new company, said the firm will be a customer-oriented concern which will sell, design, install and service such things as uninterruptible power supplies, energy management systems and metering services.

"Many CEI customers have needs and concerns different from days gone by," Greben said. "Our new company demonstrates the Illuminating Company's interest in the customer and ability to satisfy specialized electrical needs and concerns."

Greben said Dynamic Energy Ventures will also look to existing firms doing business in these areas for their expertise in helping fulfill its goals.

- more -

The new company is to be entirely self-supporting. Any financial losses, or profits, will be the responsibility of CMI's share owners, not customers, since the share owners are taking the risk in setting up the company.

Greben, who had been CMI's manager of Industrial Marketing, will be assisted by two Illuminating Company energy specialists including Max Volk, who has been named vice president. They're already seeking office space in the downtown Cleveland area.

In recent years, many electric utilities have diversified into numerous fields, including attempts to meet new customer concerns, but Greben says the CMI subsidiary appears to be the broadest customer-oriented diversification move yet made by any utility.

Minnegasco

June 7, 1984

Honorable Tom Luken
Chairman, House Small Business Subcommittee
on Antitrust and Restraint of Trade
U.S. House of Representatives
Washington, DC 20515

Dear Mr. Luken:

Minnegasco appreciates this opportunity to respond, for the hearing record, to an issue raised during your Subcommittee's hearing on regulated monopolies' competition with small business held on May 22, 1984.

Minnegasco is a natural gas distribution company serving over 500,000 customers in Minnesota, South Dakota and Nebraska. We also merchandise residential appliances as well as provide customer appliance repair service through two non-utility business segments.

In testimony presented to your Subcommittee, Mr. Harold Hager of Farm and Gustafson Plumbing and Heating, Inc. of Mankato, Minnesota alleged that Minnegasco engages in unfair and anti-competitive marketing practices with respect to our merchandising and customer service operations.

We submit, for the hearing record, that these allegations are untrue. Minnegasco's marketing practices have been carefully reviewed by the Minnesota Public Utilities Commission in several recent rate cases. Our Marketing practices are conducted within the permissible boundaries established by the PUC. We would be happy to provide you with copies of Commission orders which relate to these practices, if you desire to see them.

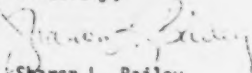
Aside from the close scrutiny given our activities by the PUC, small businesses such as Mr. Hager's are amply protected by state and federal antitrust and consumer protection laws, with which our company is in total compliance.

Furthermore, contrary to Mr. Hager's assertions, Minnegasco strongly supports the small business community. To stimulate competition, we provide cooperative advertising funds to appliance dealers such as Mr. Hager who compete directly with us. Minnegasco feels that healthy

competition, even at the expense of our own share of market, will increase the sale of gas appliances overall and benefit all natural gas consumers. We would also note that over 50,000 of our natural gas customers are small business and we depend on their economic well being for revenue.

Thank you for permitting us to present the facts about our marketing efforts. Please let us know if we may provide you with any further information.

Sincerely,


Sharon L. Bailey
Director of Marketing



Carl Cummins, III
Director of Government Relations

GVB/pk

Donll CORPORATION

11828 N.E. 112th STREET

KIRKLAND, WASHINGTON 98033

(206) 821-3888

Honorable Thomas Luken
Chairman of the Sub Committee Anti-Trust
and Restraint of Trade Activity Sub-Committee
House Small Business Committee
Room 2361 RMOB
Washington, D.C. 20515

MANUFACTURERS OF
FURNACE PIPE & FITTINGS
•
HEATING & AIR
CONDITIONING EQUIPMENT

Dear Sir:

This letter is in reference to the May 22, 1984 Utility Marketing Practices Hearing, and I would like it entered in to the official record.

I was a small business man operating in the greater Seattle area for over 21 years, running a Company (Gas Appliance Service, Inc.) that sold and installed all types of gas equipment. I sold the business 5 years ago and am now involved in the distribution side of the market place.

Being associated for that many years near and with the local Gas Utility (Washington Natural Gas Company) I formed some very strong attitudes as to the Gas Company being involved in the merchandising and leasing market. They were and still are, all very positive. The Gas Company has always been very supportive of all their dealers. They the Gas Company advertise very heavily and steadily in all the news media: newspapers, radio, TV, mail flyers, and bill stuffers. This method in turn generates much business not only for the Utility, but also for all of us in the gas industry. They the Utility are in a sense our biggest supporters, for we as small business men could not afford and are not inclined to advertise gas products to the public to such a large degree. This advertising rouses the public interest in the products involved and in turn generates much business our way also.

The Washington Natural Gas Company leasing program is also an excellent one, with much advertising being done in that area too. When the Gas Company sells or leases a piece of equipment generated by their advertising efforts, they in turn sub-contract to us the dealers all of their installation work, be it central heating, water heating, cooking equipment, etc. There-fore not only do they generate sales business for us via their advertising, but also hire us to install equipment that they have themselves sold or leased. Obviously that gives us the dealer the best of both worlds.

I hope the above helps you to understand why I feel so strongly about the Utility Companies in this country staying in the marketing field.

Sincerely yours,

A. V. Petruccelli

A. V. Petruccelli

Lodestar Refrigeration Company

June 6, 1984
our ref. # 159

Honorable Thomas Luken
Chairman-Sub Committee
Anti-Trust and Restraint of Trade Activity
Sub-Committee-House Small Business Committee
Room 2361 RHOB
Washington, D.C. 20515

Dear Mr. Thomas Luken,

We would like this letter to be on official file in protest against the elimination of in house marketing practices of utility companys. These practices refer to the May 22, 1984 utility marketing practices of merchandising and leasing.

I, Lloyd Burningham, am president of Lodestar Refrigeration Company Inc. There are six persons under my employ, effecting some thirty family members.

Lodestar Refrigeration Company Inc. is currently being sub-contracted by a local utility company as well as privately soliciting business. We have not experienced any difficulty in working with or competing against our local utility. In fact, the relationship has been a very positive one. It is our belief that the utilities are progressive marketing organizations that investigate and promote the most effective equipment for our nations changing needs.

In closing, I am a private contractor involved in all aspects of the competitive contracting business and have found the utility company a viable business partner and a fair competitor.

Sincerely,

Lloyd Burningham

Lloyd Burningham
president

dpg/lb

708 North 198th Street • Seattle, Washington 98133 • (206) 546-1968